## INDEX.


| | Page |
|---|---|
| Statement of Facts | 1–11 |
| First Syndicate Agreement | 2–4 |
| Second Syndicate Agreement | 5 |
| Agreement between Davis, Phillips, and Herbert & Mines | 4 |
| Stockholdings at the bringing of this suit | 6 |
| Errors Assigned | 11 |
| Argument | 12–37 |
| The company (appellee) has no right to any relief | 12–19 |
| Members of syndicate cannot sue company to sue for alleged wrong done to them | 19–24 |
| The company has not authorized this suit | 24–26 |
| Herbert & Mines should have been made parties | 26–27 |
| It was error to decree cancellation of deed | 27–36 |
| Conclusion | 37–38 |


### Law or Cases Cited.


| | |
|---|---|
| Anderson, &c. v. | 16 |
| Arkansas, &c., Co. v. Farmers, &c., Co. | 17 |
| Bagley v. Robinson | 24 |
| Bagley v. Saunders | 31 |
| Barr v. Ry. Co. | 17 |
| Blair v. Whitney | 16, 29 |
| Clark v. American Coal Co. | 16 |
| Crawshay v. Thorne | 19 |
| Dunmore (M) Co. v. Dunmore | 19 |
| Elkins v. U. S. M. M. Co. | 16 |
| Fagan v. Wicks | 17 |
| Flume Silver Mining Co. v. Hunt | 32 |
| Gillespie v. New Amsterdam Co. | 24 |
| Foster v. Supreme | 17, 19 |
| Fort Madison Bank v. Allen | 17 |
| Harrison v. Pueblo Trade (M) Co. | 17 |
| Hawkins v. Barney | 35 |
| Hawley v. Lansing | 17 |
| Hutchinson v. Hooper | 19 |
| Jamieson Print v. Woolrich Woo Co. | 17 |
| Jessup v. (M) Cent. R. Co. | 30, 34 |
| King v. Barnes | 17 |
| Land v. Julius Lauchheimer, &c., Co. | 29, 33 |
| Mahaska v. Robinson | 17, 19 |

Page

McChesney's Appeal ..... 29, 32
Manchester, &c., vs. Burlington, &c., Co. ..... 17
Old Dominion, &c., Co. vs. Lewisohn ..... 14, 28, 29, 30, 31, 32
Parsons vs. Hayes ..... 17
Robinson vs. Osborne ..... 16
Seymour vs. Spring Forest Assn. ..... 17
Shields vs. Barrow ..... 26, 28
Spalding vs. North Milwaukee Town Site Co. ..... 17
Stanton, &c., vs. Pixee ..... 17
Swift vs. Smith ..... 17
St. L., F. S. & W. Ry. Co. vs. Terrell ..... 17
Thornton vs. Ry. Co. ..... 17
Tompkins vs. Quarry Assn. ..... 17
Wallerius vs. Chenault ..... 17
Wood vs. Carey Water Works ..... 17
Yates vs. U. S. Bond, &c., Co. ..... 29, 31

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1912.

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## No. 87.

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NORMAN H. DAVIS AND CHARLES T. PHILLIPS, APPELLANTS,

vs.

THE LAS OVAS COMPANY, INCORPORATED, APPELLEE.

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### Statement.

In December, 1903, or January, 1904, appellants, Davis and Phillips, residing at the time in Havana, secured an option to purchase about four thousand acres of land in Cuba for ten thousand ($10,000) dollars. They met Benjamin Miess in Havana and told him about the property. Miess told them he thought he could interest some people in the property. Davis and Phillips came to Washington to try to sell the property, and Miess introduced them to George C. Held. They told Held of their option (P. R., 25). A number of meetings took place and the following paper was executed (P. R., 25, 26, 47, *et seq.*):

In

Duplicate.

"This memorandum of agreement by and between *the parties signing the same,* witnesseth:

"*Whereas, Charles T. Phillips* and *Norman H. Davis,* of Havana, Cuba, and *Hilary A. Herbert* and *Benjamin Micou,* of Washington, D. C., under the firm name of *Herbert & Micou, have secured an option* on a tract of land in Cuba containing 4,000 acres, more or less, the said land being the southern portion of the estate known as 'Las Ovas,' which estate contains 7,000 or 8,000 acres and is known as the property of the Widow Tarafa; the said 4,000-acre tract, the subject of this agreement, being situate in the Province of Pinar del Rio, south of the Western Railroad of Havana and extending to Lake Negrito;

"*Whereas,* if this 4,000-acre tract of land is suitable for the profitable raising of citrus fruits, oranges, lemons, grape fruit and the like, and a clear title can be obtained to the same, it is the desire of *all the parties* to this *agreement* that a corporation be formed under the laws of one of the States of the Union, to have its main offices at Washington, District of Columbia, for the purpose of acquiring this 4,000-acre tract of land and disposing of the same in ten-acre or other suitable-sized lots for groves of oranges, lemons, grape fruit, or the like; *it is agreed* as follows:

"That Messrs. *Phillips* and *Davis* and *Messrs. Herbert & Micou* will acquire this tract of land for a company to be organized for the purpose above mentioned, for the sum of twenty-five thousand ($25,000) dollars, $12,500 in cash on delivery of the deed of transfer, and $12,500 payable in twelve months, *and 40 per cent of the stock of the company* which is to be formed for the purpose of acquiring, developing and disposing of this property, said company to be organized upon general lines as follows:

"To have a capital stock of one hundred and fifty thousand ($150,000) dollars, 40 per cent of which, or $60,000 worth of stock to be given to Messrs. Phillips and Davis, and Herbert & Micou, *as compensation for securing the land and the preliminary work of getting up and incorporating the company afterwards to be organized;* the remainder of the $150,000 of stock, viz., 90,000 dollars, to be disposed of to the subscribers thereto for one-third of its face value, or $30,000.00; $25,000.00 of this money to go to the purchase

of the lands and $5,000 to be used as an expense fund as directed by the company, for the purpose of effecting sales of lots into which 4,000 acres shall be divided; this $90,000 worth of stock to be taken by the subscribers at one-third of its face value upon the following terms:

"One-half (½) payable down and the other half payable if necessary at the end of twelve months from the date of subscription.

"*It is further agreed* that in case it is desired by the persons subscribing to $60,000 of the $90,000 of stock, the remaining $30,000 will be taken by Messrs. Phillips and Davis and Herbert & Micou, to be divided between them as follows: $10,000.00 to Charles T. Phillips, $10,000 to Norman H. Davis, and *$10,000 to Herbert & Micou;* but as these last-named parties would own between them the $60,000 of the stock to be given for the purpose of promoting the company, and this $30,000 additional would give to them a controlling interest in the stock, they are only to take said $30,000 of the stock if it is desired that they do so by the other stockholders; or they are willing to take such portion thereof as the other stockholders may be willing that they should have.

"We the undersigned hereby bind ourselves, our heirs and assigns to take the number of shares of stock subscribed to by us to be paid for at one-third (⅓) of its face value, one-half (½) down and one-half (½) at the end of the year, if the second payment is necessary, upon the following conditions:

"That the hereinafter-named subscribers will select a person to go to Cuba without delay to examine the land and to investigate the title to the same, and in case a good title can be secured and the land is found to be suitable for profitable culture of citrus fruits—oranges, lemons, grape fruit, and the like—then this agreement to be in full force and effect, but otherwise to be null and void; and in case a good title cannot be secured, or the land is found to be unsuitable for the purpose for which it is intended, under the tenor of this agreement, then the persons who were to receive the $60,000 shares of the promoters' stock shall bear the necessary expenses of the trip to Cuba of the person selected by the subscribers hereto to make the investigation thereof."

| | Number of shares subscribed. Nominal value, $1,000 each. |
|---|---|
| Chas. T. Phillips } Norman H. Davis } | 60 shares. |
| As promoters' shares. | |
| Chas. T. Phillips | 10 shares. |
| Norman H. Davis | 10 shares. |
| Geo. C. Reid | 30 shares. |

This agreement was not to be binding unless approved after examining the property (P. R., 214).

The above instrument is incomplete as to the parties. The original was signed, or certainly agreed to, by one Billings for six shares and by "Herbert & Micou" (P. R., 40, 86, 167, 209).

Just after the above agreement, to wit, February 5, 1904, Davis, Phillips, and "Herbert & Micou" signed an agreement, drawn up by Micou (P. R., 87 and 226), by which Davis & Phillips were to receive two-thirds and Herbert & Micou one-third of all over $15,000 received for the property, whether money or stock. That agreement is as follows:

"The Jefferson, Richmond, Virginia,
"Richmond, —— —, 190–.

"Whereas there is now under consideration the organization of a corporation to acquire, develop and dispose of land in Cuba for orange growing and other purposes and the parties to this agreement who purpose being stockholders in said corporation have agreed or will agree with the other proposed stockholders of said corporation to acquire for and to deliver to the corporation when organized for $25,000 some 4,000 acres of land part of what is known as the Las Ovas tract in Pinar del Rio Province, Cuba, and whereas Charles T. Phillips and Norman H. Davis have an option on this land for $15,000, it is hereby agreed between Charles T. Phillips and Norman H. Davis as parties of the first part and H. A. Herbert and Benj. Micou, under the firm name of Herbert & Micou, as parties of the second part that any sum in excess of $15,000 paid for this land by the corporation or the subscribers to its capital stock shall be divided as follows—⅔ to be divided between the two parties of the first

part and ⅓ to go to the parties of the second part. Should the parties to this contract take stock in the corporation instead of money for the whole or any part of the excess over $15,000 to be paid by the corporation for this land then that such stock is likewise to be divided ⅔ between the parties of the first part and ⅓ to the parties of the second part. Agreed upon this 5th day of February, 1904.

"(Signed)

"NORMAN H. DAVIS,
"CHAS. T. PHILLIPS,
"HERBERT & MICOU,
"By BENJ. MICOU."

This agreement speaks of the option price as $15,000. Micou does not claim that he did not know that this was more than the price at which Davis & Phillips had their option. The $15,000 was the amount agreed by Davis, Phillips and Micou to be fixed as the price upon which the profits were to be figured and shared with Herbert & Micou.

Micou was selected by all the parties interested to go to Cuba and examine the property and have the title looked after. Reid also went, and after a thorough examination of the property by all the parties it was agreed to include additional property.

Davis secured an option to take this additional property on March 16, 1904 (P. R., 56).

Another agreement was thereupon entered into between the syndicate composed of Reid, Davis, Phillips, and "Herbert & Micou" on March 19, 1904, as follows (P. R., 90):

*"This memorandum of agreement by and between the parties signing the same, witnesseth:*

"That Charles T. Phillips and Norman H. Davis, of Havana, Cuba, and Colonel Geo. C. Reid, Hilary Herbert and Benjamin Micou, of Washington, D. C., under the firm name of Herbert & Micou, agree to purchase a tract of land in Cuba containing five thousand acres of land more or less, said portion being in the northern part of the estate known as 'Las Ovas' which estate is the property of the Widow Tarafa.

"The said five thousand acres subject to this agreement are situated in the Province of Pinar del Rio.

"That Messrs. *Reid, Phillips, Davis, Herbert & Micou, will acquire* this tract of land *for the formation* of a company to be organized for the sum of $34,000 which sum is to be paid, half in cash on delivery of the deed, and the other half paid in twelve months, and 40 per cent of the stock of the company to be formed.

"The company is to have a capital stock of $150,000, 40 per cent of which or $60,000 worth of stock to be divided equally between signers of this contract. Colonel Reid will have $15,000 of this stock; Messrs. Herbert & Micou will have $15,000 of this stock; Mr. Davis will have $15,000 of this stock and Charles T. Phillips will also have $15,000 of this stock. The remainder of the $150,000 worth of stock to be subscribed for by the people signing this agreement in proportion to the amount of shares subscribed *each one agreeing to pay sufficient money to pay for half of the land now, and the balance at the maturity of the mortgage,* provided, that there shall be an expense fund of $5,000.00 and each share shall pay its proportionate part as necessary and as is called for by a majority of the stock.

"Charles T. Phillips hereby subscribes for 22 shares stock.

"Colonel Reid subscribes for 35 shares of stock.

"Mr. Micou subscribes for 17 shares of stock.

"Mr. Davis for 10 shares of stock.

"Captain Billings has six shares of stock *which if not paid for, will be taken by the parties subscribing in proportion to their stock.*

"For the purpose of facilitating business and until the formation of the company, it is agreed by all parties that the property is to be placed under the name of Mr. Benjamin Micou who will deed it to the company as soon as same is formed, and Mr. Micou hereby acknowledges receipt of the checks of the different promoters for the stock that they have subscribed to.

"Havana, Cuba, March 19th, 1904.

"(Signed)

"CHAS. T. PHILLIPS,
"NORMAN H. DAVIS,
"GEO. C. REID,
"HERBERT & MICOU,
"By BENJ. MICOU.

"Endorsed on back: 2nd agreement."

It will be noticed from this final instrument that the parties signing it *"agree to purchase"* the property; that they *"will acquire this tract of land"* not for an existing company, but *"for the formation of a company to be organized."* The promoters' stock is divided equally between the signers, Reid taking one-fourth, though the first agreement provided for a division of one-third each to Davis, Phillips, and "Herbert & Micou."

Every share of stock in the proposed company is taken or provided to be taken by the members of the syndicate. There is to be an opening, *sub modo,* to let in Billings for six shares, but if he does not take them they are to be taken *"by the parties subscribing in proportion to their stock."* One of the syndicate is to take the title until the company is formed.

The parties to the agreement are to pay for the stock, pro rata, sufficient to pay for the property and provide an expense fund of $5,000.

Davis secured a valuable adjoining lake property for $1,000, which he turned in without profit either on it or the additional property embraced in the above agreement, making the total purchase price $35,000 (P. R., 28, 92, 93).

Billings did not come in and Davis subsequently took his six shares (Reid, P. R., 41) and sold the right to them, the company not being then chartered, to Dr. Z. T. Sowers, making a profit on his sale to Sowers.

The par value of the stock was $1,000 per share.

Application was made for a charter by all the syndicate and Dr. Sowers, and it was chartered early in June, 1904.

The property was conveyed to one Escalante, an employee of Davis and Phillips, and from Escalante to Micou.

Upon the organization of the company Micou conveyed to it.

The stock was all issued to the syndicate, except the Billings six shares, which were issued to Sowers, Davis having sold the right to them to him (P. R., 233).

Phillips sold ten shares of assessable stock to Parker and Ricks, and they not paying the assessment it went into the treasury of the company.

After the stock was issued there were various transfers. The stockholding at the time of bringing this suit was as follows (pp. 99, 235-37):

| | Assessable. | Promoters. | Total. |
|---|---|---|---|
| Reid: | | | |
| (Including one share which he gave to his secretary, and one to his son to qualify them as directors.) | | | |
| Original subscription | 35 | 15 | |
| Bought from Phillips | 6 | 8 | |
| Bought from Herbert & Micou | 9 | 3 | |
| | 50 | 26 | 76 |
| Davis: | | | |
| Original subscription | 10 | 15 | |
| Bought from Phillips | 6 | 7 | |
| Bought from Herbert & Micou | 8 | 3 | |
| | 24 | 25 | 49 |
| Herbert: | | | |
| Original subscription | .. | 9 | 9 |
| Sowers: | | | |
| Bought from Davis | 6 | .. | 6 |
| In treasury of company: | | | |
| Bought by P. & R. from Phillips and failed to pay assessment | 10 | .. | 10 |
| Grand total | | | 150 |

The auditor of the trial court reported that all the stock that Davis bought from Herbert & Micou was assessable, but he is undoubtedly in error (P. R., 99, 100, 97). Davis positively testifies that three of these shares ($3,000) were promoters' (p. 100), and Reid, though called in rebuttal to contradict Davis in other matters, does not dispute as to this, though Reid had the stock books and transfers, and on page 97 of the printed record will be found Reid's receipt to Davis, showing that his assessable stock was only 24 shares, so that his other 25 shares (including this three) were promoters'.

Reid testified that Davis and Phillips told him that the

price named in the syndicate agreement was what was to be paid the owner for the property. Davis and Phillips both denied this (pp. 94, 170), but admitted they did not communicate that they were to get the property at a less price, and Davis admitted that the taking of the deed first in the name of Escalante was partially to keep Reid from knowing.

The partnership of Herbert and Micou, through Micou, were parties to every agreement. The signature is "Herbert and Micou, by Benj. Micou." Hilary A. Herbert, the other partner, actually had $9,000 of the promoters' stock at the institution of this suit. His partner, Micou, through the agreement in the firm's name, also received some of the cash difference between what was paid the owner for the property and what was paid by the syndicate on their stock.

Reid, as secretary and treasurer, was sent by appellee to Havana in March, 1905, to see about the deeds to the property, and about March 25, 1905, learned that the owner of the property received $20,000 for it (P. R., 31).

On May 22, 1905, a special or called meeting of the directors was held, and authorized the employment of an attorney to bring suit if necessary against Davis and Phillips. The meeting was composed of Reid (holding a majority of the stock), his son, his clerk, and Sowers (P. R., 34).

On June 28, 1905, another special meeting of directors was held and proceedings were authorized. There were present Herbert, Reid, his clerk, and Sowers. No notice was sent Davis of either meeting, though he had been notified of other meetings (P. R., 34, 202, 203).

Reid, who controlled the company and was its secretary and treasurer, after knowing all about the price paid for the land to the owner, still treated Davis' stock as valid and wrote Davis about the assessments on it. Spoke of taking up the question of getting additional land for the company with Davis and of joining with Davis in buying some of the stock that Phillips had sold to Parker and Ricks. Wrote

Davis that he was glad he was coming to Washington. The letters were very friendly indeed (P. R., 150, 151).

Davis came to Washington and was met by process in the suit Reid had ready for him.

Neither Herbert nor Micou were made parties, and Herbert took part in the special meeting that authorized suit against Davis and Phillips, holding at the time $9,000 of the promoters' stock that he got by the agreement between Davis, Phillips, and Herbert & Micou, through Micou.

Both Herbert and Micou, through the partner Micou, were parties to every agreement.

The property was valuable (P. R., 216).

The object of the suit is to cancel all the stock of Davis and Phillips.

The result of the suit if maintained will be to make Davis bear practically the whole burden, as Phillips has sold his stock.

The bill is so drawn as to make it appear that there were other stockholders than the syndicate, and omits the fact that "Herbert & Micou," partners, through Micou, shared in the secret profits (P. R., 87, 98, 99, 112, 131, and 133).

The evidence shows that there were no stockholders except the syndicate, and that no other stockholders were contemplated than the members of the syndicate—one member dropped out and Davis sold the right to these shares to Sowers. Sowers simply took the place of Billings in the syndicate.

Reid, "Herbert & Micou," and Sowers, who took the place of Billings, were just as much promoters as Davis and Phillips.

The suit is simply an effort of a part of the promoters to use the company to sue other promoters (Davis and Phillips) for an alleged deception upon other members of the syndicate, or promoters, in the hopes of getting a different and greater relief than could have been gotten in suits as individuals, to wit, the cancellation of stock.

The Court of Appeals of the District of Columbia in its opinion held that the entire stock held by Davis should be canceled—his twenty-four (24) shares of assessable stock because undisclosed profits went into them; his twenty-five (25) shares of promoters' stock, which was openly agreed upon, as a punishment and penalty for taking other profits not agreed upon, and in addition that appellants, Davis and Phillips, should pay the sum of $1,546.54, with interest from November 25, 1908, and said court so adjudged in its decree of June 1, 1910.

From said decree and opinion this appeal is taken.

## Errors Assigned.

The court erred:

I. In not dismissing the bill of complaint, when the evidence showed that the plaintiff was not entitled to the relief prayed for, had no right to bring the suit, and that the suit was not legally authorized.

II. In not dismissing the bill for the failure to make Hilary A. Herbert and Benjamin Micou defendants.

III. In decreeing the cancellation of any of the stock held by Davis.

IV. In decreeing the cancellation of the twenty-five (25) shares of promoters' stock, part of the $60,000 held by Davis, about which there was no secret.

V. In decreeing the cancellation of twenty-seven (27) shares of stock as assessable stock, when Davis had only twenty-four (24) shares of assessable stock.

VI. In decreeing the cancellation of eleven (11) shares of stock that Davis purchased from Micou or "Herbert & Micou."

VII. In decreeing that appellants, Davis and Phillips, should pay in money $1,546.54.

## ARGUMENT.

### I and II.

### The Bill Should Have Been Dismissed

**Because:**

1. *The appellee (hereafter called company) proved no right to the relief prayed for.*

The company was merely a receptacle for the property, a creature erected for the convenience of the syndicate. The syndicate instead of taking the property in their own name put it in a company, which company was themselves, and only themselves, and gave it back to themselves in the shape of a certain number of shares of stock.

Appellants, Davis and Phillips (hereafter called by name), had an option on property; they mentioned the matter to Benjamin Micou; he became interested in the venture, and with a view to disposing of the right introduced Davis and Phillips to Geo. C. Reid and Billings. It was agreed by the syndicate to take the property, if approved of after examining it, and eventually to put it in a company when formed. That company, however, was to be entirely composed of the syndicate. Every share of stock was taken in advance by the syndicate.

The final agreement, after the property was examined (P. R., 90), provided that Phillips, Davis, Reid, Herbert & Micou *"agree to purchase a tract of land in Cuba;"* that they would "acquire this tract of land *for the formation* of a company." Forty per centum of the stock was to go one-fourth to Herbert & Micou, one-fourth to Davis, one-fourth to Phillips, and one-fourth to Reid. The last named had demanded and been allowed an equal share before making the final agreement. Reid gives the following reason for

sharing in the promoters' stock, though he was a party to the first agreement (P. R., 48-49), in which he was not to share.

"After I had been to Los Ores to see the property I said to Davis, Phillips, and Mieou that I thought I should share in the non-assessable stock, as well as Herbert & Mieou, inasmuch as I had to pay so much more toward its purchase; *that I was willing that Phillips and Davis should have promoters' stock; they had been the ones who originated the proposition and brought it to our attention*" (P. R., 208). As to the remainder of the stock the agreement provides, "The remainder of the $150,000 worth of stock *to be subscribed by the people signing this agreement.*"

Phillips, Reid, Mieou (for Herbert & Mieou), and Davis subscribed for all the stock except six shares. These six shares were set aside for Billings, who was a party to the first agreement, if he wished to continue. As to this six shares, it was provided that if Billings did not take them they would be taken by "*the parties subscribing in proportion to their stock.*"

Billings did not come in and Davis took his six shares (P. R., 41), without objection on the part of the others, and sold the right to them to Sowers. It was immaterial to the company what the property cost. If it can be distinguished from the syndicate it simply gave them all its stock for the property. It made no difference to the company as a separate entity from the syndicate whether the property cost one dollar or one million, for the syndicate agreed for their shares "to pay sufficient money to pay for half of the land now and the balance at the maturity of the mortgage, provided there shall be an expense fund of $5,000, and each share shall pay its proportionate part as necessary and as is called for by a majority of the stock."

The syndicate instead of taking the property in their own names simply put it in the company and took it back in the form of all of the stock of the company. The whole thing was a mere form or paper transaction and in no way changed the real ownership.

In the first agreement the same amount of stock, viz., $150,000, less 40 per cent promoters' stock, was to be given for the property, at a valuation of $25,000, to the subscribers, who were to pay therefor the cost of the property, and an expense fund of $5,000, as was to be given in the final agreement for a larger property, at a valuation of $34,000. And when it was concluded to embrace still additional property, after the said final agreement, the company gave no more for it.

The only interested parties were the syndicate. They had to contribute enough to pay for the property and provide an expense fund.

Now, Reid claims that Davis and Phillips deceived him as to what was to be paid for the property. They deny this most emphatically; and it seems rather strange that they would have made false statements in the presence of Micou (P. R., 35), against whom no charge is made and no suit is brought, though his father-in-law and partner, Herbert, was president of the company and participated in the directors' meeting that directed suit against Davis and Phillips, and at the time had $9,000 promoters' stock, which he got through the dealings of his partner with Davis and Phillips. Micou knew that less was to be paid the owner for the property than the price at which the syndicate was to buy (P. R., 87). Reid, after he knew what the property cost, could hardly have thought, then, that Davis had made false statements to him, for he wrote him affectionate letters and was considering entering into other transactions with him (P. R., 150-151). Were his letters sham and hypocrisy? Then, can his word be taken as a preponderance against both Davis and Phillips?

As to Sowers, Davis simply sold him the right to take the Billings six shares. That was certainly a matter entirely between Davis and himself. Micou was present here also (P. R., 23). The company had nothing to do with the transaction and had no interest in it. At best for Sowers, as

counsel for appellee said in his brief below, "*Sowers became Billings, for every legal or practical intent or purpose, and stands in all respects in his stead.*"

The question is then presented, if we admit, for the purposes of this point, that Davis and Phillips did deceive some of the syndicate, What has the company to do with that?

Can the company in such a case as this, where the syndicate put the property in its name and took it back in the form of all its stock, bring suit for a deception upon some members by other members of the syndicate when the public was not only not brought in, but could not be brought in, as the company had no stock to sell the public?

Certainly no reason can be given why either Reid or Sowers can use the company to sue for any injury they may claim that Davis and Phillips did them.

The authorities, both text writers and cases, are to the contrary.

This court in the recent case of Old Dominion Copper Mining & Smelting Co., &c., *vs.* Lewisohn, 210 U. S., 206, has decided that suit in such a case cannot be maintained by the company.

In that case the bill expressly alleged that Bigelow and Lewisohn took $750,000, secret profits, without the knowledge of the syndicate.

Here it is alleged that Davis and Phillips received $15,000, secret profits, unknown to the syndicate. (The evidence also shows that "Herbert & Micou," partners, through Micou, received a part of the secret profits.) (P. R., 87.)

As to this, this court said in the Lewisohn case:

> "Whether or not there was a subordinate fraud committed by Bigelow and Lewisohn, on the agreement with them, as the petitioner believes, is immaterial to the corporation. * * * Bigelow and Lewisohn, it is true, divided the stock received for the real estate now in question. *But that was a matter between them and the syndicate.*"

In the Lewisohn case, just as in the case at bar, it was alleged that some member of the syndicate took advantage of other members and took profits from the company unknown to all the syndicate. In that case, just as in ours, all the syndicate were to share in the company's stock, the only difference being that in our case the syndicate were to take all the stock, while in the Lewisohn case $500,000 of stock was from the inception of the plan to be issued to the public after the company was formed.

The court held that even this issuing of stock to the public did not of itself give the company any right to sue, saying:

> "If there was a wrong, it was when the innocent public subscribed. * * * For it is only by virtue of the innocent subscribers' position and the promoters' invitation that the corporation has any pretense for a standing in court."

The decision in the above case is sustained by the authorities.

Morawitz on Corporations (2d Ed.), sec. 202.

When directors issue the whole stock of the company for property worth less than the par amount no one is injured in the least.

Cook, Corporations (6th Ed.), sec. 651.

Blum vs. Whitney, 185 N. Y., 232 (1906):

When all the stock of the company is turned into another company in exchange for the stock of the latter, and the promoters are the only ones interested, though the stock is afterwards sold, the promoters cannot be held. The court said:

> "They dealt wholly with themselves, as sellers and buyers, organizers and corporation. *If fraud had been practiced by any one of the organizers upon*

*those associated with him, the cause of action would have vested in the party injured."*
Cook, Corporations, sec. 651, p. 1888.

Stratton, &c., *vs.* Pines, 126 Fed., 968 (1904); aff'd 135 Fed., 449:

When all the stock of a corporation is issued in payment for property the vendor cannot be held liable for misrepresentations as to the value of the property.

See also:

Foster *vs.* Seymour, 23 Fed., 65.
McCracken *vs.* Robinson, 57 Fed., 375.
Du Pont *vs.* Tilden, 42 Fed., 87.
Wood *vs.* Corry Water Works, 44 Fed., 146.
Fort Madison Bank *vs.* Alden, 129 U. S., 373.
Barr *et al. vs.* N. Y., L. E. & W. R. Ry. Co., 125 N. Y., 263, 273.
Seymore *vs.* Spring Forrest Asso., 144 N. Y., 333.
Thornton *vs.* Wabash Ry. Co., 81 N. Y., 462, 467.
Parsons *vs.* Hayes, 14 Abb. N. C. (N. Y.), 419, 434.
King *vs.* Barnes, 109 N. Y., 267, 268.
Insurance Press *vs.* Montauk Wire Co., 103 App. Div. (N. Y.), 472.
Higgins *vs.* Lansing, 154 Ill., 301, 331, 336.
Spaulding *vs.* North Milwaukee Town Site Co., 106 Wis., 481, 488, 489.
Garretson *vs.* Pacific Crude Oil Co., 146 Cal., 184.
St. L., F. S. & W. Ry. Co. *vs.* Tierman, 37 Kan., 666, 683.
Walburne *vs.* Chouault, 43 Kan., 356, 361.
Arkansas, &c., Co. *vs.* Farmers, &c., Co., 13 Colo., 587.
Tompkins *vs.* Sperry Jones, 96 Md., 560, 583.
Swift *vs.* Smith, 65 Md., 428, 435.
Merchants & M. S. B. *vs.* Burlington C. & I. Co., 41 S. Eastern R. (W. Va.), 390.

Clark *vs.* American Coal Co., 17 L. R. A., 557, 561 (Iowa).

Divine *vs.* U. S. M. M. & Co., 38 S. West. R., 93, 98 (Tenn.).

*In re* Ambrose L. R., 14 Ch. D., 390, 395, 396, 397, 399 (English).

Salomen *vs.* Salomen, L. R. (1897) A. C., 22 (Eng.).

In Foster *vs.* Seymour, *supra*, Wallace, J., says (p. 66):

> "There was no fraud upon the corporation. At the time the scrip was exchanged for the mining property, the trustees were all there was of the corporation. There were no stockholders, unless they were stockholders. What was done was done by the corporation. By the exchange the corporation got the mining property, and gave it back to those from whom it got it, divided into 100,000 shares of the nominal value of $100 each."

In McCracken *vs.* Robinson, *supra*, the Circuit Court of Appeals, in describing a similar situation, says (p. 377): "While directors in name they were principals in fact," and later on the opinion condemns the building up of a theory "by confounding names with things and forms with substance."

*In re* Ambrose, *supra*, James, L. J., says (p. 395):

> "In my view the company only gave back in substance that which it was getting, and *the fraud* was *not between the vendors and the Company*, the purchaser, but was a thing calculated to delude people into believing that the shares when got were something more valuable than they really were.
>
> *"What was taken back was the very thing that was given in exchange for it, calling it by different names and dividing it into different shares."*

Colton, L. J., on page 399, says:

> *"The remedy is a remedy of each purchaser of shares, if there were any such, who was deceived by the representations made by his vendor."*

There is no legal difference between the holder of an option and a full owner of land.

Densmore Oil Co. *vs.* Densmore, 64 Pa., 49.
Cummings *vs.* Beavers, 103 Va., 230.

It was claimed on behalf of the company that the question of dismissing the bill was not properly raised. Exactly what was meant is not perceived. If a plaintiff has not proved a case entitling it to the relief prayed for it is not entitled to any decree and the bill must be dismissed. Any decree entered in such a case is erroneous. Such questions can be presented at any time and anywhere in the trial court and in the appellate court.

2. *Neither Reid, who absolutely controls the company and its directors, nor Sowers can use the company to sue for an alleged wrong done to them by Davis and Phillips.*

The syndicate agreement affords no basis of claim on the part of the company.

The syndicate agreement was wholly between the parties thereto.

Hutchinson *vs.* Simpson, 92 App. Div., N. Y., 382.
Blum *vs.* Whitney, 185 N. Y., 232, 241, and cases above.

The formation of the company, the taking of all its stock, and the putting of the title to the property in it were all merely the carrying out of the syndicate agreement.

Equity looks at the substance and not at the form of things. There is nothing here for the company to sue for.

Thompson on Corporations, 3d Ed., sec. 3997:

The board of directors cannot fritter away its funds in litigation in respect of their own individual rights in the corporation.

As the trial judge said in his opinion (P. R., 230):

> "At the time the final agreement and subscription was made, March 19, 1904, the understanding was that Phillips, Davis, Reid, and Herbert & Micou (partners) were to turn over the land to the company for $34,000 (subsequently increased to $35,000) and forty per cent of the stock of the corporation, *i. e.*, $60,000, which stock was to be divided between them in four equal parts. In this respect, all these parties were 'promoters,' and the stock taken by each was 'promoters'' stock, and a profit to each for launching the enterprise." (See Contract, P. R., 90, 91.)

3. *The company has not authorized this suit.*

The suit was authorized at a special meeting of the board of directors, of which Davis, who was a director, was given no notice. He was notified of all other meetings except the two special meetings held with reference to bringing suit against him (P. R., 34, 202, 203, 204).

The law is well settled that no action of a special meeting of the board of directors is valid unless all the directors are notified, even though the presence of the absent ones could not have changed the result.

Mr. Thompson, in his work on the Law of Corporations, recognized as one of the best authorities on the subject, volume 3, section 3936, says:

> "When the meeting is a stated one the time and place of which is fixed by some by-law or regulation, no notice of it is necessary, but when it is a special or called meeting, all the members must be notified of it. * * * The right of all the directors to notice is founded on the right of being present for the pur-

poses of consultation, of which right a minority cannot be arbitrarily deprived by a majority. It follows that proceedings at a special meeting held by a bare majority of the members of a board of directors of a corporation, without notice to the other members, *are void*, although all those present voted in favor of the action taken, and the result would have been the same had the other members been present."

It is true that Davis had given Reid a power of attorney to represent him at meetings of directors, but this did not avoid the necessity of notice for several reasons:

*a.* Such power of attorney is a nullity.

Thompson on Corporations, volume 3, section 3909:

> "A power of attorney from one director to another to represent him at meetings of the board is illegal and void."
>
> *Idem*, volume 3, section 3925.

*b.* The power of attorney from Davis to Reid, even if valid, could not be used by Reid in such a matter as a suit against Davis. Such use could not have been intended by Davis, and would be a fraudulent use of the same.

*c.* The power of attorney had never been considered or acted on as rendering it unnecessary to send notice to Davis of meetings, but only to represent him if absent. Notice had been sent him of every meeting prior to these.

The Court of Appeals took the ground that the power of attorney was a waiver on Davis' part and that he was estopped.

Upon what ground is Davis estopped? Can it be conceived that Davis ever dreamed that the power of attorney could or would be used to bring suit against him?

The law is that any special meeting held without notice to a member is a nullity.

Not only this, but it was never, before these meetings, considered that Davis should not be notified. Notice was always, before this, sent him. The power of attorney was only to represent Davis if not present. He was entitled to notice, so that he could be present, if he desired. The power simply authorized Reid to represent him at meetings if absent. It in no way waived his right to notice, which he continued to receive until these meetings.

Again, to fail to notify Davis and order suit against him and leave out his partner in the enterprise, Herbert, who took part in the meeting, though he was equally liable with Davis and Phillips, through his partner, Micou, because Herbert was Reid's intimate friend, was not only inequitable and unjust, but was a fraud on Davis.

Reid, who controlled the company and its directory at the time of the meeting, was writing Davis most affectionate letters (P. R., 150, 151), and yet he had authorized suit against Davis and kept his friends Herbert & Micou out of it.

As Mr. Thompson says, each director is entitled to be present and have a chance of discussion.

His proxy to represent him is only in case he is not present. It cannot be treated as a waiver of notice. His right to notice and to be present is one thing. His proxy to represent him if not present is another and different thing.

It was contended that the president had a right by virtue of his office to bring this suit.

In the first place the president, Herbert, was legally just as liable to suit as Davis and Phillips for his firm, through his partner, Micou, shared to some extent at least in all profits, and Herbert had $9,000 of promoters' stock when suit was brought, and surely a court of equity would not allow him to sue others and not himself.

In the second place, it appears that the suit was brought by authority of the board of directors in a called meeting, of which Davis had no notice.

In the third place, Reid gave all the information upon

which suit was brought and swore to the bill, not the president, Herbert (P. R., pp. 35, 36). It nowhere appears that Herbert brought or directed the suit as president.

Finally, a president of a bank or similar corporation may bring suit about ordinary corporate business, and the authorities relied on by appellee are of this character, but it is not believed that any authorities can be found which authorized the president to bring suits of this sort on his own motion. If such were the law any president could ruin the corporation by involving in it ruinous litigation.

4. *Herbert and Micou should have been made parties.*

The fourth ground urged for the dismissal of the suit is the failure, and, though the evidence and proceedings showed the propriety and necessity, the refusal of the plaintiff to make Hilary A. Herbert and Benjamin Micou, composing the firm of Herbert & Micou, parties defendant.

There is no question, no dispute that Herbert and Micou participated with Davis and Phillips in all profits, secret and otherwise (Agreement, P. R., 87).

If there is any liability it is due from Herbert and Micou, as well as from Davis and Phillips. Herbert and Micou disposed of their stock except $9,000 of promoters' stock still held by Herbert, some being bought by Davis and some by Reid. Even the stock bought from Herbert and Micou is directed to be cancelled and redounds to the benefit of the $9,000 held by Herbert, though the plaintiff treats Herbert and Micou as free from blame. Concisely stated, Davis, Phillips, and "Herbert and Micou" receive certain profits in stock and money. The stock of the company is in part assessable, in part not assessable. Davis buys some of Herbert and Micou's stock of both kinds. Reid does the same. Davis and Reid also buy all of Phillips' stock. The cash profit, which was the only secret profit received, was divided between Davis, Phillips, "Herbert and Micou." "Herbert

and Micou" reside within the jurisdiction of the court. Herbert still holds $9,000 of the promoters' stock.

Davis is required to surrender for cancellation $49,000 of stock, part of which he bought of Herbert and Micou, and to pay $1,546.54 in cash. Result: Phillips escapes practically free; Herbert escapes free; Micou escapes free; Davis alone is held. He is required to surrender all the stock he originally held and also all he bought from Phillips and "Herbert and Micou," his partners in the whole transaction. And Herbert, who still holds his profit of $9,000 of stock, actually shares in what is taken from Davis.

Does not the mere statement of the facts show the absolute necessity of making Herbert and Micou parties? Can such inequitable and one-sided result have the approval of a court of equity?

General Reid was a marine officer. Colonel Herbert was once Secretary of the Navy. He and Reid are warm friends. Reid, controlling the company and its directory, seeks to let his friend escape. Will equity aid him and, in doing so, commit a great injustice? Upon what ground can a court of equity allow some of the parties to escape and throw the whole burden on one?

The trial judge, with whom on this point the Court of Appeals agrees, says (P. R., 228):

> "*Undoubtedly* Herbert and Micou would have been proper parties defendant, and, under the equity practice as it existed in England, prior to the adoption of the 32d order of August, 1841, would have been necessary parties. This order, however, which is substantially rule 51, of the Rules of Practice, adopted by the Supreme Court for the courts of equity of the United States, renders it possible for a plaintiff who has a joint and several demand against several persons, to proceed against one or more of the persons severally liable."

It is not perceived what bearing rule 51 has on this case. The rule, clearly, relates only to contract demands. It can-

not be tortured into meaning that if several parties have taken and shared in undisclosed profits some of them can be sued and others left out, when all are within the jurisdiction of the court, and the result would be to put the entire burden on one and actually allow one promoter to share in what was taken from another.

Certainly, in a case of this sort, if only a part are sued each one can only be held for the profits received by him.

As the plaintiff refused to make Herbert and Micou parties and make the action joint against all, it is extremely unjust and inequitable to require Davis separately to surrender $49,000 of stock and to pay money in addition. Why should Davis suffer this heavy penalty alone, for the stock is valuable (P. R., pp. 216 and 221), and Phillips escape for a small cash sum and Herbert and Micou escape free?

If the suit can be maintained equity and justice can be done only by making them all parties.

The above principles are fully sustained by the authorities. Thompson on Corporations, section 473:

> "In equity, the object is to do complete justice to all, therefore *all who concurred in a misapplication of funds in promoting, ought to be charged with the loss and not throw the whole burden on a part.* For otherwise, as was said by V. Chancellor Park, the others who participated in the fraud, would have the benefit of its being brought back."

This is exactly the injustice done in this case. The $49,000 of stock held by Davis ordered surrendered and the money ordered to be paid by him adds greatly to the value of the stock held by Herbert.

This court has recently said that this cannot be done.

In Old Dominion Copper Mining Company, etc., *vs.* Lewisohn, *supra*, the court, in affirming the dismissal of the bill, said:

> *"Here the members of the syndicate, although members of the corporation, are not joined and it is sought to throw the burden of their act upon a single one."*

In Shields *vs.* Barrow, 17 Howard (U. S.), 130, the general rule as to necessary parties is

> "persons who not only have an interest in the controversy, but an interest of such a nature that a final decree cannot be made without either affecting that interest *or leaving the controversy in such a condition that its final determination may be wholly inconsistent with equity and good conscience.*"
>
> Approved in Barney *vs.* Baltimore, 6 Wall. (U. S.), 280.

In Jessup *vs.* Illinois Cent. R. Co., 36 Fed., 738, the rule is thus stated:

> "If the defendants actually before the court may be subjected *to a liability under the decree, more extensive or more direct than if the absent parties were before the court, that of itself will in many* cases furnish a sufficient ground to enforce the rule of making the absent persons parties."

The court gives as one of the reasons why "Herbert & Micou" were not necessary parties, that "Micou, on the institution of this suit had parted with his stock, and *since the decree appealed from does not charge the defendants with liability for the secret profits of Micou, they are in no way prejudiced by the failure to include him as a party*" (P. R., 249). This is exactly what the decree did do. It forfeited the eleven ($11,000) shares of stock Davis got from Micou.

As to not making Herbert a party, the court further says that Herbert did not know of his partner's participation in such profits (P. R., 249). Before taking any testimony Herbert knew (P. R., 221) his partner knew all the time, and, legally, this is the same as if Herbert knew (Agreement, P. R., 87).

It was claimed for appellee in the Court of Appeals that the question of Herbert and Micou being necessary parties was not properly raised. The trial court considered the question properly raised and passed upon it (P. R. 228).

Before any testimony was taken, Herbert, the president of the company, was informed by Phillips in a letter (P. R., 222) that there was a "written agreement signed by Phillips, Davis, Herbert & Micou, Mr. Micou signing for your firm * * * that whatever possible wrong could be charged to Phillips and Davis would also be made against Herbert & Micou." The letter informed Mr. Herbert where he could see this written agreement. The evidence at an early stage showed that they should be made parties to accomplish equity and prevent injustice.

## III.

## It Was Error to Decree Cancellation of Stock.

If, by giving a different name to the same thing, by some strange legal fiction the company may be allowed to sue about matters wholly between the syndicate promoters, what is the proper recovery?

Not cancellation of the stock. The company had agreed to give the same amount of stock, under the first agreement, for 4,000 acres, at the price of $25,000, as it did under the second agreement for additional land at the price of $34,000, and when still more land was added at a price of $1,000 it gave nothing more.

Neither Davis nor Phillips nor "Herbert & Micou" got any stock from the company with secret profits. All its stock was going for the property, no matter what the price. Nor did they get any stock from the company by money paid by it for the property.

If the company can sue it can only be for the money received as secret profits. This money did not come from the company or the public as subscribers for its stock. It came

from the syndicate promoters, who paid for their stock sufficient to pay for the property. The situation is not altered by the syndicate paying the last payment into the company and then paying it out in the name of the company.

As the company has only sued Davis and Phillips, though "Herbert & Micou" were within the jurisdiction of the court, it is not equitable to make Davis and Phillips pay more than their part.

It may be true that, in exceptional cases one or more may be sued, in a case like this, for the secret profits received by a combination of several; but there must be some reason for leaving out the others.

Equity will surely not allow the plaintiff to purposely leave out some and make victims of a part without good reason.

The supreme purpose of a court of equity is to do equity. Not in some cases, but in all cases.

Thompson on Corporations, section 473:

> "In equity, the object is to do complete justice *to all, therefore all who concurred in a misapplication of funds in promoting ought to be charged with the loss, and not throw the whole burden on a part.* For otherwise, as was said by V. Chancellor Park, the others who participated in the fraud, would have the benefit of its being brought back."

Old Dominion Copper Mining Co. *vs.* Lewisohn (*supra*):

> *"Here the members of the syndicate, although members of corporation, are not joined and it is sought to throw the burden of their act upon a single one."*

Shields *vs.* Barrow, 17 Howard (U. S.), 130.
Barney *vs.* Baltimore, 6 Wal. (U. S.), 280.
Jessup *vs.* Illinois Cent. R. Co., 36 Fed., 738.

Thompson on Corporations, section 465:

"The measure of the recovery in equity is only the net secret profits."

McIlhenny's Appeal, 61 Pa. St., 188:

In the case of a promoter "it is not damages in a case like this that equity gives, it is restoration of the thing wrongly taken, namely, the money received."

In the well-considered case of Emma Silver Mining Co. *vs.* Grant, 11 Law Reports Ch. Div., 918, it was held that in estimating secret profits allowance must be made for all expenses incurred.

"Herbert & Micou," through Micou, received some of the secret profits (Agreement, P. R., 87; also pp. 97, 100, 112).

So far as the company is concerned, not having made "Herbert & Micou" partners, it must be presumed they received their full part.

The company must be consistent. It cannot leave out "Herbert and Micou," thus treating them as innocent, and at the same time hold Davis and Phillips for all the secret profits, some of which was certainly received by "Herbert & Micou," through Micou.

Am. & Eng. Enc. of Law, vol. 7, p. 22.

Littel *vs.* Julius Lansburgh Furniture Co., 96 Va., 540.

It is merely mixing and twisting things to say secret profits received from the company bought any stock held by Davis. All the stock was to be paid for the property, whether it cost much or little. So that enough money for the property and $5,000 expense fund was furnished, it mattered nothing to the company who put it up. Its position was simply: Here's all my stock for the property and expense fund. Whether some members of the syndicate put up more than their part was nothing to the company.

Whether stock shall be cancelled or the secret profits in

money refunded must depend in each case upon the facts disclosed.

This case is not like Yeiser *vs.* U. S. Board and Paper Co., 107 Fed. R., 340, so much relied on.

In that case the promoters organized a company and sold property to it. The public was then invited to and did subscribe and pay for stock. The promoters subscribed for some of the stock and paid for it with the purchase money illegally gotten from the company.

In our case the public neither subscribed for any stock nor were asked to do so. The promoters got no money from the company or the public.

It is submitted that to cancel stock held by Davis would be inequitable, and that the remedy, if any exists, is to compel restoration of the money received by Davis and Phillips less all expense.

## IV.

It was error to decree the cancellation of the $25,000 promoters' stock held by Davis, about which there was no secret.

There was no secret about the $60,000 of promoters' stock. Both the first and final written agreements provided that the syndicate promoters should receive it (P. R., 46, 47, 48, 49, 90). Under the first agreement it was to be divided between Davis, Phillips, and "Herbert & Micou" as compensation *"for securing the land and the preliminary work of getting up and incorporating the company."* Under the final agreement Reid was to share, and the consideration was that Davis, Phillips, Reid, and "Herbert & Micou" *"will acquire this tract of land for the formation of a company to be organized."*

There is no question that what was to be done for the stock was done.

The company, if it had any right to sue, might possibly ask for a rescission of the contract, offer to return the property, and recover its stock, putting all the parties in *statu*

*quo*. But, surely, it cannot keep the property and recover what was openly agreed to be paid for it.

The authorities relied on, Barney *vs.* Sanders, 16 How., 535, and Walker *vs.* Beal, 9 Wall., 743, were cases of ordinary trustees, whose compensation was a matter of grace, not of right; where the allowance of compensation and the amount or the disallowance depended entirely upon the services performed and the faithfulness or unfaithfulness of the trustees' actions.

In the case at bar the compensation was a matter of contract, and the thing to be done having been done the company cannot both keep the property and recover what was agreed to be paid.

The company recognizes the $26,000 of this promoters' stock held by Reid, being his original 15 shares, and eight he got from Phillips and three from "Herbert & Micou," and the $9,000 held by Herbert, and yet seeks to cancel $25,000 of this same promoters' stock held by Davis, being his original 15 shares, and seven he got from Phillips and three from "Herbert & Micou."

This would be a great thing for Reid and Herbert, to keep their $35,000 of this stock and, through the fiction using of the company's name, to cancel their fellow-promoter Davis' $25,000.

The theory the court proceeded on in cancelling this stock is that equity can inflict pains and penalties and mete out punishment and take away from one party to a contract what was agreed to be paid him and let the other party keep property and not pay for it.

Thompson on Corporations, section 8287:

> "As in the case of directors, the thing which the rule condemns is the taking of *secret* profits by the promoter from the corporation which he promotes. It does not inhibit the taking of *open* profits."

*Idem*, sections 459, 463:

While a promoter may be charged with secret profits he is entitled to his expenses.

In the case of McIlhenny's Appeal, 61 Pa. St., 188, which was a case in which a promoter was charged with secret profits, the court uses this language:

> "It is not damages in a case like this that equity gives, it is restoration of the thing wrongfully taken, namely, the money received, or an equal sum and interest."

In the well-known case of Emma Silver Mining Co. *vs.* Grant, 11 Law Reports, Ch. Div., 918, where Grant was held liable for the amount of secret profits he had made, it was also held that in estimating the amount of such profit he was entitled to be allowed all sums expended in the promotion.

All the cases we have been able to find negative the idea that a court of equity can penalize and fine in such cases by taking away what was openly agreed to be given.

## V.

It was error to decree the cancellation of twenty-seven (27) shares as assessable stock when Davis had only twenty-five (25) shares of assessable stock.

There is not the least question that three ($3,000) of these twenty-seven shares were part of the sixty thousand dollars promoters' or non-assessable stock. These three shares Davis purchased from Micou. Davis testified positively to this (P. R., 100). Reid, the secretary and treasurer of the company and the real prosecutor of this suit, was called in rebuttal of Davis, and contradicted Davis in several particulars, but did not contradict him as to this. Reid had the books and knew that Davis was correct as to these three shares. After Davis had all the stock bought by him trans-

ferred by Reid on the books of the company he received from Reid a receipt for his assessment on all of his assessable stock, viz., 24 shares (P. R., 97). This shows conclusively that Davis had only 24 shares of assessable stock.

## VI.

It was error to decree the cancellation of eleven shares ($11,000) of stock that Davis purchased from Micou, or "Herbert & Micou," Micou paid something on this stock, certainly at least $1,200.00 (P. R., 181). He borrowed it from Reid, but this made no difference to the company.

There is no question that Davis, Phillips, and "Herbert & Micou" were parties under a written agreement, and that "Herbert & Micou," through Micou, shared in the secret profits (Agreement, P. R., 87; also pp. 97, 100, 112). The company did not make "Herbert & Micou" parties defendant, as it should have done, and did not call on them for any responsibility. Having thus recognized Herbert & Micou as without fault, it must follow as a necessary sequence that it recognized their stock as valid and is estopped from asking for the cancellation of any of it bought by Davis.

Reid, under the guise of the company, having let out his friends Herbert and Micou, cannot attack Herbert & Micou stock held by Davis.

Parties are not allowed to take inconsistent positions in legal proceedings.

Am. & Eng. Enc. Law, vol. 7, p. 22.

Littel vs. Julius L[illegible] Furniture Co., 96 Va., 540.

If any stock, then, could be cancelled the above eleven shares must be deducted, leaving in Davis, only sixteen shares that could possibly be cancelled in any event.

Certainly all of the Micou stock cannot be cancelled when

he had paid something, certainly $1,200, not secret profits, for it.

## VII.

It was error to decree that in addition to cancelling stock appellants, Davis and Phillips, should pay $1,546.54.

This was arrived at by charging them with $1,200 paid them by Micou, for "Herbert & Micou," and $1,333 paid Davis by Sowers for the Billings six shares (P. R., 235).

The company can make no claim for these two sums. It was not a party to the transactions nor in any way hurt by them.

Appellee claims that this objection cannot be made because there was no exception to the auditor's figuring.

This is an appeal from a decree, not from the auditor's report.

The court decreed that the company should have from Davis and Phillips $1,546.54 to arrive at which they were charged with, $1,200 and $1,333, that the company had no interest in, and it is submitted that where a decree takes from defendants and gives to the plaintiff what the evidence shows the plaintiff is not entitled to the point can be made anywhere.

The auditor's report was simply something the court directed for its own convenience. It is not an ordinary accounting of claims allowed or disallowed against an estate by an auditor settling accounts.

It was for the court to decree what was right and if in a case of this sort it had decreed against defendants that to which the plaintiff was not entitled the defendants can have it set aside on appeal.

In a case of this sort no exceptions to an auditor's report are necessary. It is for the court to decide on the evidence what its decree shall be. It cannot delegate this duty to the auditor.

Suppose the auditor had reported $1,000,000 against the defendants without any evidence to support it, and the court had so decreed. Would the defendants have to pay it because of no exception to the auditor's report? Would they have no right to appeal from the decree which had no evidence to support it?

The auditor was simply giving his opinion on certain matters for the benefit of the court. It was for the court to accept the auditor's views or not as it thought right. If the court erred in such matter the appeal is from the court's opinion and decree and not from the auditor's report.

## Authorities Relied on by the Appellee Company.

The authorities relied on by the appellee company are unlike the case at bar. They were not cases where some members of the syndicate who formed the company attempted to use the company's name to sue for an alleged deception by some members of the syndicate on other members thereof. They were cases where the public was brought in as subscribers and were deceived or defrauded, as in the cases relied on of Yeiser *vs.* U. S. Board, &c., Co., 107 Fed., 840; Erlanger *v.* New Sombrero Phosphate Co., 3 App. Cases, 1218, and Gluckstein *vs.* Barnes (1900), A. C., 240.

All the cases relied on by appellee were cited in the Lewisohn case, *supra*, and many others, and the same contention was made in that case as was made below in the case at bar.

Counsel for the Old Dominion Copper Mining & Smelting Co. contended in their brief (page 49) as follows:

> "The syndicate members were to become stockholders and did become stockholders as joint adventurers *pursuant to the original plan*, and if the corporation had been composed only of them and the promoters, the corporation, as representing their collective rights, could have maintained their suit for the breach of the fiduciary duty of promoters."

But this court decided that under such circumstances, which were practically the same as in the case at bar, the contract and all the relations were matters entirely separate from the company, and it could not sue for any subordinate fraud between members of the syndicate.

As to the cases relied on and the contention that the company could sue for the benefit of a part of the syndicate, this court said:

> "The argument for the petitioner is that all would admit that the promoters (assuming the English phrase to be well applied) stood in a fiduciary relation to it, if, when the transaction took place, there were members who were not informed of the profits made and who did not acquiesce, and that the same obligation of good faith extends down to the time of the later subscriptions, which it was the promoters' plan to obtain. (In our case there was no intention and it was not possible to have other subscribers, as all the stock was taken by the syndicate or promoters, *my words.*)
>
> "It is an argument that has commanded the assent of at least one court, and is stated at length in the decision. But the courts do not agree. There is no authority binding upon us and in point. The general observations in Dickerman *vs.* Northern Trust Co., 176 U. S., 181, were *obiter*, * * * *Whether or not there was a subordinate fraud committed by Bigelow and Lewisohn on the agreement, as the petitioner believes, is immaterial to the corporation.*"

## CONCLUSION.

It is respectfully submitted:

1st. That there was no cause of action in the appellee corporation, the deceit alleged to have been practiced being entirely personal to the syndicate and in no way injurious to the corporation.

It was to get certain property and give all its stock to the syndicate for getting it, whether it got less property at the price of $25,000, or more at the price of $34,000.

The syndicate was to put in sufficient money to pay for the property and provide an expense fund of $5,000. So far as the corporation is concerned, the syndicate fulfilled all conditions and did all they were required to do. As this court has said, if there was any subordinate fraud committed by some of the syndicate on other members thereof, that was purely *"a matter between them and the syndicate."* Old Dominion Copper Mining Co. *vs.* Lewisohn, *supra.*

2d. If the corporation had cause of action, then Herbert and Micou, who were within the jurisdiction of the court, should have been made parties and not cast, practically, the entire burden on Davis, their partner in the entire transaction. Equity and justice required this, and the corporation, through Reid, who owned and controlled it, should not be allowed to single out Davis and Phillips, and shield Herbert and Micou because they were Reid's friends.

3d. This was not a case for cancellation of stock. Such relief will work hardship and injustice. The proper relief, if any, is to restore the money taken by each, since only a part were made defendants.

4th. There can certainly be no cancellation of the twenty-five (25) shares of promoters' stock, part of the $60,000

held by Davis, which was provided for in the written agreements and about which there was no secrecy.

5th. If there can be cancellation of assessable stock it cannot apply to the eight shares Davis purchased from "Herbert & Micou," through Micou, for the corporation, by not making either Herbert or Micou defendants, recognized them as free from fault and hence cannot question the validity of their stock. This leaves only sixteen (16) shares of assessable stock in Davis which can be cancelled in any event.

6th. There can be no decree against Davis and Phillips for $1,546.54, because, to arrive at this sum, Davis and Phillips were charged with $1,200, received from Micou, who was their partner, familiar with and sharing in the whole transaction, and with $1,330 received by Davis from Sowers. The company was not interested in either of these transactions.

SAMUEL A. PUTMAN,
J. K. M. NIRTON,
*Counsel for Appellants.*

IN THE

# Supreme Court of the United States

OCTOBER TERM, 1912.

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No. 87.

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NORMAN H. DAVIS and CHARLES T. PHILLIPS, *Appellants*,

*v.*

THE LAS OVAS COMPANY, INCORPORATED, *Appellee*.

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## BRIEF FOR APPELLEE.

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The facts of this case are substantially as follows:

In the latter part of January or the first of February, 1904, the appellants, in the city of Washington, informed Gen. George C. Reid that they had an option on 4,000 acres of land in Cuba, belonging to Madam Acosta, the widow of one Tarafa, sometimes referred to in the record as Madame Tarafa, at the price of $25,000; that they proposed to form a stock company for its purchase, of which 60 shares were to be promoters' stock, going partly to

them and in part to the law firm of Herbert & Micou, but telling him nothing of any other profit than their said promoters' shares (Rec., p. 25). This project of the formation of a corporation to take the land had been formed before Reid was approached (Phillips, 166). A prospectus was drawn up by Phillips, set forth at pp. 46-7 of the record, stating that it was proposed to form a company with a capital of $150,000 to develop the 4,000 acre tract of land, which would cost $25,000, one-half of the purchase money to be paid in cash and one-half in 12 months; that $5,000 would be necessary for the expense of exploitation; that the promoters were to receive 40 per cent of the stock, the remaining $90,000 of the stock to be given to those who should subscribe the $15,000 then needed, and obligate themselves to pay the remaining $15,000 if found necessary.

At or about the same time a subscription agreement was drawn up by Phillips, a copy of which, incomplete as to signatures, is to be found at pp. 47-49 of the record, stating that Phillips, Davis and the firm of Herbert & Micou had secured an option on the 4,000 acre tract; that they were to acquire the tract for a company to be organized for the sum of $25,000, $12,500 payable in cash on delivery of the deed and $12,500 in 12 months, the total capital stock to be $150,000, 40 per cent of which was to be given to Phillips, Davis and Herbert & Micou "as compensation for securing the land and the preliminary work of getting up and incorporating the company afterwards to be organized," the remaining $90,000 of the capital stock to be disposed of to the subscribers at one-third of its face value, or $30,000, $25,000 of this money to go to the purchase of the land and $5,000 to be used as an expense fund, as directed by the company, for the purpose of effecting sales of the lots, etc., the persons who were to receive the pro-

moter's shares to bear the expenses of a trip of a representative of the subscribers to examine the land, etc. The copy of this agreement introduced in evidence (Record, pp. 47-9) shows its subscription by Phillips and Davis for the entire 60 shares of the promoters' stock, with an additional 10 shares subscribed for by Phillips, 10 shares by Davis and 30 shares by Reid, the original of which agreement was also signed by Herbert & Micou (Davis, p. 86), and by one Billings (Phillips, 167; and see Reid, 40), the last named participating, also, in the selection of Micou to visit Cuba and examine the land as the representative of the subscribers (Record, pp. 26-7).

It will be noticed that in this, the written contract between the parties, upon which their several subscriptions were sought and obtained, the 40 per cent or $60,000 of promoters' stock was to be given *"as compensation for securing the land,* and the preliminary work of getting up and incorporating the company."

Immediately after the presentation of the foregoing prospectus and the signing of the foregoing contract, Phillips, Davis and Micou, according to the testimony of the appellants, went to Richmond for the unsuccessful purpose of endeavoring to secure a further subscription from Governor Willard, and while there an agreement, set out at p. 87 of the record, was entered into between them, reciting that Davis and Phillips had an option on the land for $15,000, and that any sum in excess of $15,000 paid for it by the proposed corporation or the subscribers to its capital stock should be equally divided between Davis, Phillips, and Herbert and Micou, one-third to each, or, if the parties should take stock in the corporation instead of money for the whole or any part of the excess over $15,000 to be paid by the corporation for the land, then the stock should in like manner be divided, two-thirds to Phillips and Davis and one-third to Herbert & Micou—the agreement bearing date February 5, 1904.

At the time of these transactions, the option held by Phillips and Davis was for 4,000 acres of land, for the price of $10,000, instead of $25,000, as represented to Reid and Billings, and instead of $15,000, as represented to Micou (Davis, 84; Phillips, 165).

After the contract was made in Washington, it was discovered through the employment of an expert (Rec., 88-9), at the expense of the corporation p. 223), that the land covered by the Davis-Phillips option did not include the best land; whereupon that option was abandoned, and on March 16, 1904, new options were obtained pursuant to an agreement between the parties concerned, including Gen. Reid, through Tarafa, son of the widow Acosta, covering the whole Tarafa tract of about 8,000 acres, for $25,000, or a portion of it, of 5,000 acres, including the better land north of the railroad, for $19,000, or that portion with a lakeland addition of about a thousand acres for $22,000. (Record, 50, 52, 89-90.) On March 24, 1904, a censo of $5,400 was discovered as possibly encumbering the land, in consideration of which the widow Tarafa abated $2,000 from the option of $22,000 above noted, and on the following day, March 25, 1904, she made a deed of the land covered by her $22,000 option, thus reduced in price to $20,000, to one Escalante, an employee of Davis and Phillips (Rec., 93) for the sum of $20,000, of which $5,000 was paid her in cash, and a mortgage taken for $15,000, payable in one year from that date. On the same date, Escalante conveyed the same land to Micou for an expressed consideration of $35,000, taking a further mortgage from Micou to himself of $2,500, payable in one year, with interest at 10 per cent per annum, which mortgage he took simply as the secret agent of the appellants, as a part of their secret profits, having himself no interest in it whatever, and being a man without property or resources (Rec., 112, 131).

Some few days prior to this consummation of the purchase, Gen. Reid, Phillips, Davis and Micou had agreed to the purchase of the 5,000 acres, not including the 1,000 lakeland addition, of which Gen. Reid had not then heard, which purchase it was represented to Reid by Davis and Phillips would cost $34,000; and, being under the necessity of going to Guantanamo upon official business, without waiting for the consummation of the transaction, Gen. Reid agreed with Phillips, Davis and Micou that each should put up his check for his respective proportion of $17,000, which it was represented to Reid would be the one-half of the purchase price of the land then payable in cash, Davis agreeing to provide for the shares of the stock subscribed for by Billings, to be divided later *pro rata* among the parties if Billings should fail to take them. Reid accordingly gave his check for $6,611.15 (Rec., 27), which was his *pro rata* share of the cash payment to be made pursuant to a new agreement entered into between the parties, dated March 19, set out at pp. 90-91 of the Record, to the effect that they had agreed to purchase 5,000 acres of land, more or less, the property of the widow Tarafa, for the sum of $34,000, to be paid half in cash on delivery of the deed and the other half in twelve months, the 40 per cent of promoters' stock to be divided, $15,000 to Reid, $15,000 to Herbert & Micou, $15,000 to Davis and $15,000 to Phillips, the remaining [redacted] of stock to be subscribed for by the parties signing the agreement, "each one agreeing to pay sufficient money to pay for half of the land now and the balance at the maturity of the mortgage," with an additional expense fund of $5,000, Phillips subscribing for 22 shares of the stock, Reid 35 shares, Micou 17 shares, Davis 10 shares, and Billings 6 shares which, if not paid for, the other parties would take pro rata, the property to be placed in the name of Micou, who was to convey to the company

as soon as it was formed, "and Mr. Micou hereby acknowledges receipt of the checks of the different promoters for the stock that they have subscribed to." (Record, pp. 90-91.) The checks thus given Micou by the appellants were mere blinds, for the purpose of deceiving Reid, with no intention that they should be presented for payment or paid, and they never were. (Rec., 181-3.) "We were not really putting up any money." (Rec., 111.)

The re-division of the promoters' stock was in accordance with the refusal of General Reid to go further with the matter unless he was allowed as much of that stock as Herbert & Micou, in view or the fact that he had come to Cuba to examine the land, and was putting up more money for the enterprise than any of the other parties (Record, pp. 38, 89-90, 109-110, 168-9).

This latest agreement, dated March 19, 1904, signed in Cuba as above noted (Record, pp. 90-91), recites that Micou had received "the checks of the different promoters for the stock that they have subscribed to." General Reid's share, on this basis of $34,000 to be paid for the 5,000 acres then contemplated to be purchased, was $6,611.15, being 35/90 of $17,000, the alleged one-half of the purchase money for the 5,000 acres which the appellants represented was to be paid in cash. Phillips put up his check, on the like basis, for the 22 shares subscribed for by him, Davis put up his check, on the like basis, for the 10 shares subscribed for by him, and Micou put up his check, borrowing $1,500 from Reid for the purpose of enabling him to make his share of the payment (Phillips, 181-3)—and yet the only money to be paid, or which was actually paid, was $5,000, one-fourth of the $20,000 for which the property was in fact being sold by Mme. Acosta. Reid understood, as all the parties knew, that all the checks were to be cashed, and that $17,000 would be paid to Madame Acosta (Phillips, 181-183; see Davis, 110-12; Reid, 27).

As a matter of fact, Reid's check, alone, paid the entire $5,000, the whole and only cash payment, and left a surplus of $1,611.15. Micou, who, the testimony of Davis and Phillips alleges, knew the real history of the transaction, borrowed $1,500, for the expressed purpose of making up the amount necessary to be paid by him, from General Reid, who gave him a check for it, $300 of which amount was refunded to Micou by Phillips, who cashed the check, and the remaining $1,200, added to the $1,611.15 left over from Reid's check, was divided by Phillips and Davis as "profits"—the $1,200 cash payment made by Micou being due from him, as between himself, Phillips and Davis, in consequence of the fact that he had subscribed for more stock than his due share of the "profit stock" (Davis, 110-11, 116, 133). The $1,200 thus paid by Micou was, therefore, not intended to go into the purchase of the land, nor in any manner for the benefit of the company, and did not do so.

In other words, having contracted for 17 of the 90 shares of the assessable stock of the company, and to pay his *pro rata* share of the alleged $17,000 necessary to make the cash payment of the purchase money, which share would have been $3,211, he pays, according to the appellants' testimony, $1,200 to be divided among them as secret profits, pays nothing to or for the Company, and yet receives from the Company, when organized, his seventeen shares, issued to him by it under the belief that he has in good faith paid therefor to it, or for its benefit in the purchase price of the land, the $3,211 agreed to be paid as the first instalment of fifty per centum of the consideration for the 17 shares.

On the return of General Reid from Guantanamo, a few days after the transaction with Mme. Acosta had been closed, Micou having then returned to Washington, Davis stated to him that an additional 1,000 acres, including the

lake, had been offered by Mme. Acosta for $1,000, and proposed that he, Phillips and Reid might take this 1,000 acres as a "side issue," to which Reid replied that the company should have the option to take it, and this was ultimately agreed to (Reid, 28-9; Davis, 92-3; Phillips, 170), Reid and Sowers being really, and the others ostensibly, assessed to make up the additional $1,000 (28-9, 223-4). As a matter of fact, this 1,000 acres, with the lake, formed a part of the tract which Mme. Acosta conveyed to Escalante on March 25, 1904, the price of which was included in the $20,000 to be paid to her, the cash installment for which had been actually paid her; and it formed, also, part of the tract conveyed by Escalante to Micou on the same day.

It had formed a part of the tract, embraced in the alternative option noted above, for $22,000, and its addition grew out of the fact that a *censo* or encumbrance upon the land had been discovered, in consideration of which Mme. Acosta had abated $2,000 of the option upon that tract and sold the 6,000 acres, including the lake, for $20,000, instead of the 5,000 acres for $19,000, which the parties had elected to take, by their March 19th agreement (Rec., 51, 65).

In May or June, 1904, Davis and Phillips visited Washington, and in the latter month (29) the complainant company was organized. During this visit, Billings electing not to take the six shares which had been subscribed for by him, Davis sold the subscription to Dr. Z. T. Sowers, stating to him that Billings could not pay for them, that Sowers could have them at the same price which Billings was to give and which all the stock had cost, coming in on the same footing with all the others, namely, on the ground floor; that the land cost $35,000, with $1,600 for expenses, to be paid proportionately, and that the proportional cost

of these 6 shares would be $1,333.33, for which amount Sowers gave him his check (Record, pp. 20-21). He further represented that the widow Tarafa had had to mortgage her property, that she had nothing but land and was compelled to have cash, and for this reason had sold this part of the estate, and that Sowers was in on the same footing with everybody else, giving the same price that everybody else had paid, and exactly the same price that the stock had cost Davis (Record, p. 21; and see Reid, 32); that $35,000 was the very lowest price that the land could be bought for, that they were very fortunate in getting it on such terms, and that it had cost the company $35,000, with an extra $1,600 divided up pro rata among the stockholders (21-2). This transaction occurred in May, 1904 (Record, 20). No money was at any time paid for or on account of the Sowers stock except that paid by him, and the stock was never issued to anyone other than himself. In other words, he was one of the original shareholders—his payment of the $1,333.33 preceding the incorporation of the company, and the application for the charter being signed by him as one of the original incorporators. See Rec., p. 217.

With respect to the allegations in the answers that Reid had assisted Davis to sell this stock to Sowers, the latter testified that Reid had nothing to do with the purchase and knew nothing of it until after it had been made (Record, p. 21), which statement is confirmed by Reid (Record, 33), and the charge is retracted by Davis (Record, p. 96).

The interposition of Escalante into the matter, as grantee of the Widow Acosta and the grantor of Micou, is alleged in the answers to have been resorted to on the advice of counsel that, because of the discovered censos, it was advisable to have an intermediary of the grant. The attorney in question, one Mendoza, testifies in chief that Madam Acosta, the vendor, insisted upon a reference to the censos

in the conveyance executed by her; that a conveyance to the ultimate purchaser which should not refer to the censos was desirable because, under such a deed, the purchaser might more readily disclaim payment of or liability for them, and that, upon his advice, while the deed from Madam Acosta to Escalante expressly referred to the censos, the subsequent deeds from Escalante to Micou and from Micou to the Company stated, only, that there were censos of which the purchaser was cognizant (Record, 65-6). On cross-examination, however, he admits that, if Micou had taken the property directly from Madam Acosta, and had then conveyed it to the Company, by a deed not acknowledging the censos, the Company would have been in the same position with respect to them as Micou was after he received the deed from Escalante (Record, 69); and, while the answers disingenuously assign only the reason stated in them for the appearance of Escalante in the transaction, Davis in effect admits (Record, 113-114), and Phillips, after much evasion, finally confesses (Record, 190), that his introduction was for the purpose of concealing from the other parties in interest the secret profit which was being made, at their expense. Mendoza, also, states that, besides the advantage of having an intermediate purchaser for the purpose of facilitating the non-acknowledgment of the censos, "the second reason was, as I believe, that Escalante was buying for one price and selling for another." (Record, 66-7.)

The fact of the deception practiced upon the innocent stockholders and upon the corporation, it will be observed does not depend for its establishment upon the relative credibility of the witnesses for and against the defendants. It is nowhere more plainly shown than by the testimony of the appellants themselves. (See Davis Record, 102-3, 105-8, 110, 111-12, 114, 115; Phillips, Record, 175-7, 180-3, 184, 185, etc.)

General Reid having been told at the time, and Dr. Sowers later, that the land had cost $35,000, that $17,500 had been paid in cash, and that the residue of the purchase money was represented by two promissory notes secured by mortgage, one for $15,000 held by Madam Acosta, and one by Escalante for $2,500, both drawing interest at 10 per cent per annum, payable quarterly, the appellant Davis, on behalf of himself and his associates in the deception practiced, proceeded to collect the interest on the $2,500 mortgage by representing that Escalante was demanding it, that he, Davis, was being importuned for it, compelled to advance it, and the like. (See letters of Davis of February 17, 1905, Record, 121-2; February 21, 1905, Record, 114, 115; May 2, 1905, Record, 161; the alleged Escalante letter, Record, 158—Escalante being unable to speak or write the English language; Davis, Record, 113.) As a matter of fact, Davis, himself, received and appropriated to his own use the moneys thus collected as interest on the $2,500 mortgage (Record, 112, 113-14, 122), and the entire principal when it was paid, in March, 1905. The question of fact between himself and General Reid as to whether he represented Escalante to Reid as one of the owners of the property, and as a member of the Acosta family, is settled by his own letters to Reid, produced in evidence. (Record, 114, 121.)

As late as January, 1905, the Company had been unable to procure possession of the deeds to the property, although writing to Davis several times for them, on which account General Reid was sent by the Company to Havana for the purpose of securing them. Notwithstanding Davis' statements, first, that he had given them to Micou, and then that he had given them to Phillips, both of whom were in the United States, General Reid eventually traced them into the possession of Davis, himself, unrecorded, and, on returning to the United States, left the deeds for record with

Arealiano, the notary, to be forwarded when recorded (Record, 29-30). Being unable still to receive them by correspondence, and the deferred payment approaching maturity, General Reid again came to Havana, in March, 1905, secured the deeds and took them to Major Runcie, an American lawyer in Havana, whose translation of them to him for the first time advised General Reid of the fact that the deed from Madam Acosta to Escalante recited a consideration of $20,000, while those from Escalante to Micou and from Micou to the Company stated a consideration of $35,000, which discrepancy Davis at the time undertook to explain by stating that a reduced amount was put into the first deed for the purpose of reducing the transfer tax to be paid to the Government (Record, 31-2). Though somewhat doubting this explanation, yet not knowing absolutely that the price was not really $35,000 (Record, 44), and being advised by Runcie that the fraud would be no defense against foreclosure under the laws of Cuba, he paid the mortgages, under fear that, if not paid, the vendors could take back the land, and the money which had been theretofore paid would be lost. (Record, 44.)

Some effort was made, by the testimony of the Cuban lawyer Mendoza, to show that a successful defense against the mortgages might have been made in Cuba, the testimony being that, upon institution of a criminal proceeding for the fraud, the criminal judge could have notified the civil judge to stop proceedings in foreclosure, and, if the criminal proceeding resulted in a conviction, the criminal judge would have enjoined the foreclosure permanently. (Record, 65, 69, 70.) The same lawyer states, however (Record, 68-70), that there was no basis for a criminal action on the face of the deeds, and no evidence was offered that the conduct of the appellees, fraudulent as it was,

would have formed the basis of a successful criminal prosecution under the Cuban law.

The entire principal of the $2,500 mortgage was appropriated, as stated, as the interest had been, by Davis to his own use. (Record, 112, 121.)

In January, 1905, according to the testimony of Davis, Micou informed him that Reid had learned of the actual cost of the property, was displeased, and that it would be better for Davis if Micou were eliminated from the transaction (Record, 131), the fact being that Reid knew nothing of the exaggerated or fictitious price until March, 1905, when the deeds were translated to him by Runcie, as above stated. Davis, however, in January, 1905, approached Reid with a statement that neither Micou nor Phillips could pay their assessments for the stock held by them, and that both would sell their holdings for exactly what they had cost them (Record, Kane, 203, 205; Reid, 211; Davis, 121), and proposed that he and Reid should purchase these shares, which was accordingly done. Phillips had sold ten of the shares held by him to Ricks and Parker, which ten shares had been bought in by the Company, and are treasury stock, his remaining twelve assessable shares being assigned by him to Reid and Davis, General Reid paying $1,800 for the shares which came to him (Record, 158), while Davis took the shares thus acquired by him from Phillips in some kind of settlement, of so uncertain a nature as to render him unable to state what they really cost him, or whether they cost him anything (Record, 131), Micou had received six of the fifteen shares of promoters' stock which went to the firm of Herbert and Micou, and had subscribed for seventeen shares, making twenty-three in all, of which Reid, under the representations of Davis, above stated, purchased twelve shares, paying $1,591 there-

for (Record, 58), while Davis took the remaining eleven shares, for which, and for Micou's alleged interest in the Escalante mortgage, he states he paid Micou $750. (Record, 131.) The purchase by Reid of his portion of the Phillips and Micou shares was upon Davis' statement to him (Reid, 211; Kane, 203-5) that the stock would be sold to him at its actual cost to Phillips and Micou, and the price paid was figured out by Kane, the Secretary of the Company, from data furnished by Davis for the purpose, as showing the actual cost to Micou and Phillips, respectively, the fact being that none of the stock had cost any of the parties anything, except the $1,200 which Micou had paid to Phillips and Davis, not for the land, nor for any purpose of the Company, but as a part of their secret profit in the transaction, and as the consideration for allowing Micou to take more of the agreed profit stock than his *pro rata* share thereof. Davis did not tell Reid that these parties had paid nothing for their stock, but allowed him to go on and buy it, upon Davis' representations above stated, Davis knowing that Phillips had paid nothing at all, and Micou only $1,200. The testimony of Davis, himself, to this fact will be found at page 120 of the Record. The data furnished by him to Kane (Rec., 223) represented Phillips, Micou and himself as having paid their full *pro rata* shares.

The following inaccuracies in the brief for the appellants will be noted:

At page 7, Davis and Phillips are represented as having secured the right to take an additional one thousand acres for $1,000, and to have allowed the company, after it was formed, to have this land without profit upon it, or upon the additional land embraced in the March 19th agreement;

the fact being that the option held by Davis and Phillips when in Washington in January, 1904, was abandoned, and a new alternative option, for different land, obtained through Romaguera, a broker, whose fee for the service was charged to and paid by the company (Record, pp. 111, 223), and the purchase of one of the tracts contained in it agreed upon by Reid, Davis, Phillips and Micou, by their written agreement of March 19, 1904 (Record, pp. 90-91), the remaining lakeland tract being added at an additional cost of only $1,000 because of the censos discovered against the entire tract, as above pointed out. Although the cash payment for the entire tract purchased, lakeland and all, was but $5,000, and was paid out of the $6,611.15 gotten from Gen. Reid by falsely representing to him that a cash payment of $17,500 was being made, Davis pretended that he had advanced $500, as one-half of the additional $1,000 charged for the lakeland tract, and actually assessed and collected this additional sum from the subscribers to the stock of the company to be formed (Rec., 28-9), against which company, when formed, it was duly charged (Rec., 223-4).

At page 5 of the brief it is alleged that "Hilary A. Herbert, the other partner, actually had some of the stock profit at the institution of this suit," while at page 13 it is further stated that "Herbert and Micou also received some of the cash undisclosed profits." There is not a syllable of testimony in support of these allegations. Herbert never, at any time, had any stock of the company except nine of the fifteen promoters' shares which were allotted to the firm of Herbert & Micou, nor is a single dollar of the cash profits pretended, or suggested, even, by any witness, to have come to his hands.

On the same page it is stated that, "after the last agreement, Davis secured a valuable lake property, adjoining the

above, for the sum of $1,000; this also he turned into the company afterwards formed, without profit." The fact is that the lake-land addition was embraced in the alternative option above procured by Romaguera (p. 56), at an added price of $3,000, this option being obtained on March 16th, three days *before* the "last agreement" in question.

So far from Davis having secured the lake property, the fact is that, after abandonment of the 4,000-acre option, the only one obtained by the appellants, upon discovering the unsatisfactory character of the land embraced in it through the services of an expert employed on behalf and at the expense of the future corporation, this lake property was embraced in the alternative option obtained for the proposed company by the Cuban real estate agent, Romaguera, also employed at the expense of and paid by the corporation (Rec., 223). This option was given March 16 (Rec., 56), and therefore was in possession of the parties three days before the agreement of March 19th (Rec., 90), electing to take the 5,000-acre option. How, after discovery of the censos, in addition to that named in it, the 6,000 acre option was substituted, at a reduction in price to $20,000, has already been stated. The option of March 16th was not only obtained by a real estate agent employed for and paid by the corporation, but was obtained two months after the complainants, by the agreement set out on pp. 47-9 of the Record, had become the employed agents of the future corporation, to acquire the land for it.

At page 20 of the brief, the bill is charged with omitting "the fact that 'Herbert & Micou,' partners, through Micou, shared in the secret profits," at p. 23, that "there is no question, no dispute, that Herbert and Micou participated with Davis and Phillips in all profits, secret and otherwise," and that Herbert and Micou disposed of their stock except

$9,000 of promoters' stock still held by Herbert," etc., that the cash secret profit, "was divided between Davis, Phillips, 'Herbert and Micou,' " and on p. 24 that Herbert and Micou were Davis' "partners in the whole transaction." An apparent consciousness of the unfair, disingenuous and unfounded character of this charge against Mr. Herbert is indicated by the fact that it is made, not against Herbert and Micou, but against "Herbert and Micou," as an idealized, artificial entity. As explicitly declared by the Court of Appeals (Rec., 249), where a like unfounded charge was made, "It is nowhere intimated in the record that Mr. Herbert knew, or had reason to know, of his [Micou's] participation in secret profits. Stockton vs. Henderson, 40 N. J. Eq., 486."

The very plain and simple facts in this connection are that Herbert and Micou were a firm of lawyers, and that Mr. Herbert as the senior member of the firm received nine of the fifteen shares allotted to it "for attending to the legal details incident to the business" (Davis, Rec., p. 86). Contrary to the allegations of the brief for the appellants—made nowhere else—he never received a single share or a single dollar of the secret profits; and that this was perfectly well known to Davis, even if the brief and discussion of the matter in the Court of Appeals unfortunately failed to secure the attention of his counsel, is shown by his own testimony as to the reason why, the manner in which and the person from whom he bought the Micou secret profit stock (Rec., 131). The Richmond contract between Davis, Phillips and Micou, though signed by the latter with the name of his firm, was not within the scope of a law partnership, and the record shows affirmatively was not understood by the appellants to have been known to Mr. Herbert. When confronted with this suit, and in the hope of using that contract as a means of inducing him

to interpose and stop it, Phillips wrote him, on behalf of himself and Davis and by the latter's authority, the letter, at pp. 221-2 of the Record, containing the following:

> "While we did make a profit on this transaction, it was in my opinion a legitimate one, and if you will call upon Mr. Putnam, our attorney, and ask him to show you the written agreement signed by Phillips, Davis, Herbert and Micou, Mr. Micou signing for your firm, you will see that whatever possible wrong could be charged to Phillips and Davis would also be made against Herbert and Micou. For our own part, I think it would be infinitely better for all concerned for this matter to be settled out of court."

The failure of appellants, by an appeal of this character, to influence the action of Mr. Herbert in his capacity of President of the complainant corporation, charged with the duty of protecting the interests of its stockholders, for whom it and he are trustees, was doubtless a disappointment to them, but, it is submitted, affords no justification for unfounded attacks upon him in the briefs filed on their behalf.

At page 14 of the brief, the transaction between Davis and Sowers is stated to have been a matter entirely between themselves, and that "the company had nothing to do with the transaction and had no interest in it." By reason of that proceeding, Sowers became, and remains, a holder of six shares of the capital stock of the company, constituting a liability against it, which it was misled into issuing by the misrepresentation of Davis that the money paid by Sowers for the shares had gone into the purchase of its land. Is it without standing in a court of equity to call its trustee or agent to account for the secret, illegal profit thus obtained by him, in violation of his duty and at its expense?

At page 13 of the brief, the corporation is represented as

having given all its stock to its promoters for the property, and that it was immaterial to the company what the property cost, because the syndicate had agreed to purchase it for the company, in consideration of its shares. But under no one of the several agreements between the parties was all the stock to be given, or taken, for the property, or for enough money, merely, to pay for it. Nor was Gen. Reid simply a promoter, nor was Dr. Sowers a promoter at all. The former, as to the thirty-five shares of assessable stock subscribed and paid for by him, was simply a shareholder, while the latter, who neither received or was to receive any promoters' stock at all, was always a mere shareholder. The company itself, which in good faith before discovery of the frauds bought and paid for the ten shares which Phillips had sold to Parker and Ricks, is itself entitled to relief, in its own interest and in its own right, against the fraudulent shares outstanding in the hands of the appellants.

## POINTS AND AUTHORITIES.

It may somewhat clarify consideration of the case to determine, from the record, what questions are brought up by the appeal.

The paragraph in the conclusion of each of the answers of the appellants (Rec., pp. 12-13, 18) is to the effect that each, in answering, "does not waive the right given to him by the order of this Court passed in this cause on the 9th day of October, 1905, to renew his motion to strike the bill from the files and quash the writ of subpoena." It is fair to assume from these recitals, as is the fact, that, upon some ground or other, the defendants did move to strike the bill from the files and quash the subpoena, and that the motion was overruled, without prejudice to the right to renew it later. The motion, however, was not renewed, nor is any ground for the proposed action apparent upon the record.

The decree of the Supreme Court of the District of Columbia, from which the case was carried to the Court of Appeals, and from the decree in the latter court affirming it, the present appeal is taken, dealt only with specific exception to the Auditor's Report (Rec., 232 238, 239, 240), which exceptions it overruled, affirming the report and giving effect to its findings. The question, discussed at pp. 7 to 10 of the brief for appellants, that the institution of the suit was not authorized by the corporation, is, therefore, not presented by the appeal.

Pages 10-14 of the brief for appellants are devoted to the question whether or not the bill was defective for want of parties, in that the members of the firm of Herbert & Micou were not made parties. This question, also, is not raised by the pleadings, by motion before the Auditor, by the exceptions to his report, or in any other manner, and, therefore, we submit, is, also, not presented by the appeal.

After considering and deciding adversely to the appellants both the foregoing questions, as though they had been properly raised, the Supreme Court of the District in its opinion (Rec., pp. 225-31) held:

1. That the defendants should account for the secret profit received by them, such secret profit being the difference between the amount paid to the Widow Acosta, and that paid by the complainant for the land in question, with interest from the date of the receipt of such profits, less any amounts paid out by them in securing the land or in forming the corporation.

2. That the complainant, at its election, might recover the secret profit as money, or might follow it in so far as it went into the stock of the Company, in which latter case the shares representing such secret profits should be delivered up and cancelled.

3. That the defendants should not be required to sur-

render for cancellation the promoters' stock received by them.

4. That the cause should be referred to the Auditor to ascertain the net amount of secret profits, and the proportion thereof invested in the stock of the plaintiff now held by the appellants, or either of them.

The Auditor (Rec., pp. 232-35) found the appellant Davis to be the holder of 49 shares, 22 of which were promoters' stock; that the remaining 27 shares represented secret profit, and that, over and above them, there remained the sum of $1,546.54 of secret profit to be accounted for in money.

The appellee, by its exceptions, raised the question as to the right of the appellants to any of the promoters' shares, which question the Court of Appeals decided in its favor, decreeing their surrender and cancellation.

The appellants by their exceptions, which will be found at pp. 229-40 of the record, raised the following questions, and none others, namely:

(1) That the Auditor erred in finding Davis the owner of 22 shares of promoters' stock and 27 assessable shares, instead of 25 shares of promoters' stock and 24 assessable shares, as claimed by him—this question being the substance of the first, second and third exceptions on behalf of the appellants.

(2) That the Auditor erred in finding that the 27 shares represented secret profits, "while the record shows that the defendants paid a large sum of money into the treasury of the complainant company as assessments or payments for said shares of stock"—this being the fourth exception taken.

(3) That the report "does not give defendants credit for large sums of money shown by the record to have been paid by them as expenses in the organization of complainant company, and for which they have never been reimbursed" —this being the fifth and final exception taken.

That, in this jurisdiction if not elsewhere, exceptions so indefinite and general as the appellants' fourth and fifth, being propositions 2 and 3, *supra*, are insufficient, and must be overruled is well established by the decisions of our courts. Haller vs. Clark, 21 D. C., 128, 133; Richardson vs. Van Auken, 5 D. C., App., 209; Smith vs. American Bonding Co., 12 D. C., App., 192.

In addition, the testimony of Davis, himself (Record, 111), shows that all expenses of the organization of the company were charged against it by him, and paid to him by it, except the expenses of Phillips and himself in coming to Washington, in January, 1904, for the purpose of attending a stockholders' meeting of the Colonial Trust Company—on the ground that, though coming to Washington for that purpose, they had embraced the opportunity, while here, of getting up the Las Ovas enterprise, upon the fraudulent basis which has led to the present litigation, and were, therefore, entitled to credit for the expenses in question. Notwithstanding this admission, and the evidence of the fact contained in the Record (p. 223), the brief for the appellants here still contends (p. 32) that the decree below was erroneous for failure to allow expenses.

No assignment of error referable to either the fourth or the fifth exception being contained in the brief, nor any argument made therein in support of them, they are doubtless to be regarded as abandoned. The Auditor's Report (Rec., 235) expressly credits all assessments paid and allows the appellee only the excess of the secret profits above them.

At pp. 14, 34, of the opposing brief, it is objected that the appellee had nothing to do with the $1,333 of profits made by Davis on the sale to Sowers. No such objection was in any manner, however remotely, made before the Auditor, or raised by the exceptions to his report. It is made for the first time, in the appellate court. It is elementary

that this cannot be done—this in addition to the fact above noted that the result of that transaction was to place into the hands of Sowers, an innocent holder, six shares of the capital stock of the company, of the par value of $6,000, for which it is liable to him and for which with the exception of some later assessments paid by him, the company received nothing.

Judge Gould having held that the so-called promoters' stock was not invalidated by the fraudulent conduct of the promoters, the appellant Davis not unnaturally sought to claim that the largest possible share of his holdings was promoters' stock. It was contended for him, accordingly, that, in addition to the 15 shares of this stock which went to him under the agreement, he should have been credited with seven shares of the stock purchased by him from Phillips as non-assessable, which credit is given by the Auditor's report, and that, in addition, three of the six shares acquired by him from Micou should be regarded as of this class, making 25 shares in all. Micou, it is true, had six promoters' shares, which with his 17 alleged assessable shares, making 23 in all, he sold to Davis and Reid under the circumstances above set forth, Davis getting 11 and Reid 12. There is nothing to show that these shares were physically distinguishable in any way, or, upon any other principle than arbitrary assumption, that Davis got three or any other number of them in the shares purchased by him.

The three disputed shares, it will be noted, are a part of those acquired by Davis from Micou. The undisputed fact is found by the Auditor that, of the 23 shares which went to Micou, six of which were promoters' shares, Davis sold 12 to General Reid and retained 11 for himself. The contention on his behalf is that, since he testified that three of the eleven were promoters' shares, and was not contradicted in rebuttal, it should now be adjudged by a court of equity

that three of the eleven shares thus acquired by him from Micou, paying only $750 for them all and for a share in the Escalante mortgage besides, should be adjudged promoters' stock, and that, of the 12 Micou shares sold by Davis to Reid, three should be adjudged to have been fraudulent shares, though their sale was made to Reid, as Davis admits, with full knowledge upon his part, and without any knowledge upon the part of Reid, of their fraudulent character, and of every fact and circumstance which made them so, as now disclosed by the record. Indeed the testimony of the witness Kane (Rec., 203) shows that the price to be paid for these shares was figured up by him upon data furnished by Davis as to their cost to Phillips and Micou, which data (Rec., 223) represented Phillips as having contributed $4,277.80 and "Micou"—not Herbert and Micou—as having contributed $3,305.57, an aggregate of $7,583.37, toward the cash payment for the land and the lake addition —the cash payment having been in fact only $5,000, and for which, including the lakeland assessment, $6,705.59 was gotten from Reid.

A very simple test is, suppose Micou, selling the 12 shares to Reid, had himself retained the remaining 11 shares; could he have been heard in a court of equity to claim, under the circumstances, that three of the twelve shares thus sold by him to an innocent purchaser were fraudulent, and, therefore, that three out of the 11 which he retained were good? And, if not, does Davis, who made the sale of the 12 shares to Reid, and himself acquired the 11 shares, with full knowledge of all the facts at the time of the transaction, stand in a better position than Micou would do if he had retained the 11 shares?

We submit that, if the Court of Appeals erred in reversing so much of the decree below as gave the appellants their promoters' stock, and if the question, therefore, were

material, the seven so-called promoters' shares obtained by Davis from Phillips should, also, be treated as assessable shares, upon the like principle. Knowing that Phillips had, at the time of the sale, but 27 shares in all, 15 of which were to his knowledge secret profit stock, he negotiates a sale of 14 of the shares to General Reid, an innocent purchaser for value, rendering them in Reid's hand valid outstanding liabilities of the Company, and, having done this, he simultaneously takes Phillips' remaining 13 shares, with full knowledge of all the facts. If Phillips had retained these 13 shares, under the circumstances stated, would he have been heard to say, in equity, that he had sold the invalid shares, either wholly or in part, to Reid, and was therefore entitled to have the retained shares, or any of them, treated as valid in his hands, in addition to those rendered valid as against the Company by his fraululent sale of them to an innocent purchaser, on the express representation that he had paid for them? And. if not, is Davis, who knowingly made the misrepresentation upon which Reid bought, and who simultaneously acquired the other 13 shares, knowing all the facts, and in such a way that he is unable to show what, if anything, he paid for them, in any better position?

If the Court of Appeals, however, was correct in holding that the appellants were no more entitled to retain their promoters' than their secret profit shares, as we submit it was, the above discussion becomes immaterial.

The theory upon this point of the District Supreme Court (Record, pp. 229-31) was that the promoters' shares were not secret, but known to all the parties in interest; that the appellees contributed to the enterprise the option on the land, and that it would not be equitable to deprive them of compensation therefor.

On the other hand, it is submitted on behalf of the appel-

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Lees, as to the first of these grounds, that the right of persons occupying a fiduciary character to compensation for their services does not depend upon the question of secrecy of acquisition, but upon that of good faith; and as to the second, that, by the very terms of the subscription agreement, prepared by the appellee Phillips (Record, pp. 46, 106) and fully known to the appellee Davis (Record, p. 106), the promoters' stock was to be given them "*as compensation for securing the land and the preliminary work of getting up and incorporating the company after it was to be organised*"; that the theory that the promoters' stock was to be given them for the option which they held not only finds no support in the testimony, but is negatived by the express terms of the subscription agreement—prepared and presented by themselves, as stated. Not only so, but as shown by their own testimony, the option which they held was for land south of the railroad, which was found, after the subscriptions to the agreement were made, to be inferior and the option to purchase it, which was the only option they possessed, was abandoned; that the option upon which the enterprise really proceeded was one subsequently obtained, for different land, and at the cost of the appellee, on the 16th of March, more than a month after the subscription agreement had been signed, the record being really without any testimony to show that the original option, upon the land south of the railroad, possessed any value, and it being admitted that nothing had been paid for it.

Under the theory of the opinion below, and as the result of its decree, the appellee and the appellants would be left in precisely the same situation as if the latter had acted in good faith throughout the transaction, had acquainted the appellee and its stockholders with the true cost of the land, had attempted no fraud against them, had honestly and legitimately performed their duties, and had not subjected

it to the present protracted and expensive litigation to defeat their now plainly proven and uncontested frauds. Such, we submit, is not the doctrine either of the law or of the equity courts.

Suppose, instead of promoter's shares, the subscription agreement had provided that the promoters should receive, say, 40 per cent of the net profits which should be realized upon the adventure; that they had pursued the same lines of conduct which are shown in the record, that $20,000 of net profits had been realized, and that the present contention were, Are they entitled to the agreed percentage or commission upon the profits for their services? Can there be a moment's hesitation or question over the determination of such an inquiry? Is it not elementary law, fixed beyond even the propriety of discussion, that neither a trustee, an agent, nor any other fiduciary is entitled to compensation for his services where he has been guilty of concealment, misrepresentation, and the grossest attempted frauds upon his principals or *cestui que trustent*, for the purpose of overreaching and despoiling them, and of enriching himself at their expense? And, if so, can there be any difference whether his compensation was fixed by the contract at a percentage of the profits, or a percentage of the proposed capital stock of the corporation?

We submit that, by the very terms of the contract under which the appellants were to receive any promoters' stock at all, it was to be in consideration of, and as their compensation for, the securing of the land and the organization of the company; that the law inexorably applies to the right to receive such compensation the condition that the duties of the agent or fiduciary shall be performed honestly, and forbids it where the services are accompanied by secret, dishonest and fraudulent practices, at the expense of the principal or other contracting party; that the appellants, accordingly, are not entitled to their promoters' stock, contracted

to be given them for the proper performance of their duty; that it is contrary to public policy, and to the settled principles of both law and equity, that a trustee or agent may experiment, fraudulently, for a known illegal and unjust advantage, retain the benefits of his fraudulent conduct if undiscovered, and, if detected, nevertheless receive all the benefit of his contract to which he would have been entitled had he acted honorably and in good faith, suffering, only, the loss of his unlawful embezzlement or misappropriation of the moneys coming into his hands through the trust and confidence reposed in him, and that so much of the decree below as permitted the appellees to retain their promoters' stock, under the undisputed facts and circumstances of this case, was erroneous and was properly reversed.

If the Court shall be of opinion that the other questions discussed on behalf of the appellants are properly to be considered upon the record in this cause, those questions are the following:

I. Should the suit have been dismissed, as not properly authorized?

II. Should the bill have been dismissed because Herbert and Micou were not made parties?

III. Was the appellee competent to maintain the suit?

## I.

The institution of the suit was authorized, as pointed out in the opinion of the Court below (Rec., p. 227), by the unanimous direction of the Board of Directors at the meeting held June 28, 1905, Hilary A. Herbert, the President of the corporation, being present and concurring. The objection is that Davis, who resided in Cuba, and who was one of the parties to be proceeded against, was a director, and was not notified to be present at this meeting (202). He

had expressly declared that it was not necessary to send him notices of the meetings of the Board, as he could not come to Washington to attend its special meetings (202-3).

Conrad Reid, the only director other than Davis absent from the meeting referred to, had been present at an earlier meeting where the same action was taken, and all the directors were in favor of bringing the suit (Rec., p. 334). The action of the directors at these two meetings will be found at page 218 of the record. The president, who concurred in the authorization, was by the by-laws empowered to perform all the duties incident to the position of Chief Executive Officer of the Company, or required by law (Rec., p. 218). This included the right to employ counsel and authorize suits. Russell vs. Savings Bank, 23 App. D. C., 398.

That the authority of the president of a corporation, alone, is sufficient for the employment of counsel in the institution of suits, is abundantly established. Beebe vs. Beebe Co., 64 N. J. L., 497; Dallas Co. vs. Crawford, et al., 18 Tex. Civ. App., 176; American Ins. Co. vs. Oakley, 9 Paige, 496; Reno Water Co. vs. Leet, 17 Nev., 203; Streeten vs. Robinson, 102 Cal., 542; Mumford vs. Hawkes, 5 Denio, 355; Ricord vs. R. R. Co. 15 Nev., 177.

He may even employ counsel and authorize suit against the Board of Directors, itself. Recamier Mfg. Co. vs. Seymour, 5 N. Y. Supp., 648:

> "When the president of a corporation executes, in its behalf and within the scope of its charter, a contract which requires the concurrence of the board of directors, and the Board, knowing that he has done so, does not dissent within a reasonable time, it will be presumed to have ratified his act." Railway Co.'s vs. Bridge Co., 131 U. S., 371, 381.

In the present case, not only was the suit authorized by the president and every officer and stockholder of the cor-

poration except Davis and Phillips, the parties to be sued, but the Company has prosecuted the suit for seven years, including its successful appeal to the Court of Appeals from so much of the decree of the lower court as held it liable to the appellants for their promoters' stock.

Even if the two meetings of the Board of Directors at which the suit was directed to be brought were technically invalid because of failure, under the circumstances, to give Davis notice, and thereby prevent suit by warning him to keep out of the jurisdiction, the fact remains that the suit was authorized by every officer and director except Davis, and by every stockholder except Davis and Phillips, the parties to be proceeded against. The claim that such a suit can not be authorized except by a duly called meeting of the Board of Directors is not supported by any authority.

## II.

Should the bill have been dismissed because Herbert and Micou were not made parties?

To this objection there are several answers.

With respect to Mr. Herbert, he received, as the senior member of his firm, 9 of the 15 shares of the promoters' stock to be allotted to it "for attending to the legal details incident to the business" (Davis, p. 86). Contrary to the allegations made first, and only, in the brief of the appellants, he never received a single share of the "profit stock," nor any of the "cash undisclosed profits." Not the slightest cognizance upon his part of the wrongdoing of the appellants, or of any one else, and still less of any participation by him in it, is anywhere pretended, or suggested, by any witness in the case, nor is there a shred of evidence in the voluminous record which can afford the slightest ground for doubt or suspicion against his integrity, throughout the

entire transaction. Nor are the appellants, or either of them, charged by the Auditor's report, or by the decree, with any accountability, however remote, for his shares.

That the consideration for which the shares of promoters' stock were to be allotted to his firm was rendered faithfully and honestly, in so far as he is concerned, is unquestioned. Can technical responsibility for the misconduct which the appellants allege his partner participated with them in committing, and which was clearly outside the partnership scope, constitute in a court of equity a defense to them against accountability for their own conceded fraudulent, secret profit derived from it?

In the second place, with respect to Mr. Micou, the complainant neither knew nor had cause to suspect at the time of instituting its suit, nor did the appellants advise it by their answers, that he was in any way concerned with any of the fraudulent practices which had been employed. The knowledge of the appellants in that regard was possessed by them as fully at the time of their answers as at the present time. The rule is well established that objection for want of parties must be made at the earliest practicable time, and that it will be disregarded, at least except in the case of indispensable parties, if not then made. Dios vs. Burchard, 10 Paige, 447, 458-9; Mechanics' Bank vs. Seton, 1 Pet., 306; Weightman vs. Critic Co., 4 D. C. App., 153; Landram vs. Jordan, 25 D. C. App., pp. 299-300. It is nowhere [redacted] in the voluminous record, being first raised in the argument before Mr. Justice Gould.

In the third place, it is not contended that the assignment by Micou to Davis was not absolute and unconditional, vesting in the latter all the title that Micou had, and leaving no vestige of interest remaining in the assignor. Why, then, should he be made a party?

"The true principle would seem to be, that in all cases where the assignment is absolute and unconditional, leaving no equitable interest whatever in the assignee, and the extent and value of the assignment is not doubted or denied, and there is no remaining liability in the assignor to be affected by the bill, it is not necessary to make the latter a party." Myers vs. Cottrell, 25 Wash. Law Rep., 721, citing Story's Eq. Pl., Sec. 153.

A and B fraudulently obtain from X a conveyance by X to B of Lot 1, which B then conveys to A. Can it be contended that B is a necessary party to a suit by X to set aside the deed?

In the fourth place, neither the report of the Auditor nor the decree appealed from charge the appellants or either of them with responsibility, or with liability, for any secret profits made by Micou, or any secret profit other than their own. They are required, simply, to surrender outstanding liabilities of the complainant corporation held by them the issue of which was obtained by their own fraudulent practices, partly to themselves originally, and partly to others from whom they acquired them with knowledge of all the facts, and that they account for any further secret profit in their possession, in money.

In the fifth place, could it benefit the appellants if Herbert and Micou were made parties? Suppose Micou were decreed to pay to the Company his secret profit, if any, realized by him in the transaction, or even that Mr. Herbert should surrender his 9 shares of promoters' stock; to what extent could that relieve Davis from the obligation to cancel the secret profit, which he holds, or relieve himself and Phillips from their liability to refund their secret cash profits?

With respect to an objection made below in argument, only, that the appellants should be required to make several, not joint, refund of their secret profits, it is, we submit, ob-

vious that, if the objection were before the Court upon the record, it is entirely untenable. With respect to the $1,200 obtained from Micou, it was paid to them, not in separate sums, but jointly. With respect to the secret profit made by Phillips out of his sale to Reid, the sale was broached, negotiated and consummated by Davis, upon whose misrepresentation that the price was the actual cost of the stock to Phillips, the profit was realized. They were partners in the perpetration of the frauds, throughout, and cannot claim the technical protection of a several liability because of any subsequent division among themselves of the proceeds of their joint transactions, even if they had made disclosure or claim thereof in their answers or in their testimony, which, however, they have not done.

## III.

The remaining question, also not raised by the pleadings, is, was the appellee competent to maintain suit for the relief sought by the bill?

The answers, the evidence, the summary of the points of contention set forth in the opinion of Mr. Justice Gould, the Auditor's Report, the exceptions thereto, the final decree, and any and every other part of the Record in the case will be scanned in vain for the slightest reference to or suggestion of this objection. It had its origin in the decision of this Court in the case of Old Dominion Copper Company vs. Lewisohn, 210 U. S., 206, decided by the Court some three months after Judge Gould's decision in the case at bar and before the hearing in the Court of Appeals.

If capable of being considered at all by this Court, notwithstanding the fact that it is a point not raised below, it remains to inquire whether the decree below is, as to the point in question, in conflict with, or supported by, the case of the Old Dominion Copper Co. vs. Lewisohn.

In that case, certain promoters had acquired certain properties for the purpose of conveying them to a corporation to be organized by themselves, at an excessive valuation. They accordingly formed a new company, composed entirely of themselves, which company, with full knowledge upon the part of every incorporator of all the facts in the case, and without concealment of any kind or character, agreed to take over the properties in question and to pay therefor 130,000 shares of its capital stock, leaving some 20,000 shares in its treasury. Some of the stock, amounting in all to a 2-15 interest in the company, subsequently passed into the hands of innocent holders, the other 13-15 remaining the property of the original incorporators, who had consented to the purchase. The suit was a bill by the corporation against the estate of one of the deceased promoters, who had acted nominally as a vendor of a part of the property to the company, acquired in his name for the purpose, but really as the representative and for the benefit of all the proposed incorporators, to rescind the sale of that portion of the property, or to recover damages for the sale, to which bill a demurrer was interposed, and sustained by the Court below. The decree was affirmed upon the specific and explicit ground that the corporation had "assented to the transaction with the full knowledge of the facts." There was no stockholder who did not know the exact facts, and all the facts, attending the proposition of sale, or who had not assented to it and taken his share of the stock given in payment—every stockholder having been a promoter and an equitable part owner of the properties acquired for the purpose, and sold to the company. But, says the Court in its opinion, at pp. 213-14:

> "If there had been innocent members at the time of the sale, the fact that there were also guilty ones would not have prevented a recovery, and even might not be

a sufficient reason for requiring all the guilty members to be joined as defendants in order to avoid a manifest injustice. Stockton vs. Anderson, 40 N. J. Eq., 486."

The manifest injustice referred to, namely, that of compelling one promoter to refund the entire excessive price, although he acted only for himself and all the other stockholders, the latter of whom knew all the facts and received and still held their share of the excess thus sought to be recovered from him alone, is wholly wanting here, where the appellants are sued for their own secret profit, only.

The theory of the bill was that the promoters, concededly trustees for the proposed corporation up to the time of its organization, continued to be trustees for later subscribers to the capital stock, which it was the promoters' plan to obtain. The Court held that the corporation was a continuing entity, from the time of its original existence, unchanged by its changing stockholder constituency; and that, as it would have been estopped while its stockholders remained the same to rescind or recover damages for the sale made to it, with the full knowledge and consent of all concerned, it remained so estopped notwithstanding that, later, a 2-15 interest in the stock was obtained by subsequent purchasers who bought without notice—the rights of these being left to be determined between themselves and the parties who induced them to purchase their stock.

The utter absence of analogy between this case and the case at bar is self-obvious. The appellee corporation was not chartered until June, 1904. At that time, General Reid was a holder of 35 assessable shares and Dr. Sowers, who neither received nor was to receive any promoters' stock at all, held 6 assessable shares, making 41 shares out of 90. It is an undisputed fact that the sale to the corporation, for $35,000, of land the actual price of which was $20,000, and the conversion to their own use by the ap-

pellants, and according to their statement by Micou, of the remaining $15,000, was wholly unknown to Reid, Sowers, or to Herbert, the holder in good faith of 9 of the promoters' shares. In such a situation, the Court says in its opinion, as above noted, "If there had been innocent members at the time of the sale, the fact that there were also guilty ones would not prevent recovery." The corporation is not estopped under such circumstances, and, therefore, the very ground upon which the Court proceeded in Old Dominion Copper Co. vs. Lewisohn is lacking. The absence, also, of analogy with respect to the injustice referred to in the opinion, has already been pointed out.

## APPELLANTS' AUTHORITIES.

With the doctrine of Blum vs. Whitney, 185 N. Y., 236, cited at p. 16 of the brief for appellant, that, when all the stock of one or more companies is exchanged for the stock of another company, and the promoters are the only ones interested, the latter are not liable to subsequent purchasers of the shares of stock of the new company, we have no quarrel, the doctrine thus deduced by appellant from Blum vs. Whitney being the same as that laid down by this court in Old Dominion Copper & Smelting Co. vs. Lewisohn, 210 U. S., 206.

Of the further authorities cited at page 17, the following are to the same effect: Foster vs. Seymour, 23 Fed., 65; Seymour vs. Spring Forest Cemetery Association, 144 N. Y., 333, 340; Parsons vs. Hayes, 14 Abb. N. C., 419, 434; Barr vs. N. Y. R. R., 125 N. Y., 263, 273; Higgins vs. Lansing, 154 Ill., 301; St. Louis R. R. Co. vs. Tiernan, 37 Kans., 633; Walburne vs. Chenault, 43 Kans., 352, 361; Thompkins vs. Sperry, 96 Md., 560, 583; Swift vs. Smith, 65 Md., 428; Merchants' Bank vs. Bellington Coal and Coke Co., 41 S. E. Rep., 390, 398; Clarke vs. Ameri-

can Coal Co., 17 L. R. A., 557; McCracken vs. Robinson, 57 Fed., 375; *In re* Ambrose Lake Co., 14 Ch. Div., 390; Salamon vs. Salamon, L. R. App. Cases, 22; Garretson vs. Crude Oil Co., 146 Cal., 184, and *obiter*, Divine vs. United States S. M. Co., 38 S. W. Rep., 98; Wood vs. Corey Water Works Co., 44 Fed., 146.

The following citations, at the same page, appear not to be relevant to the questions presented in this case: Ft. Madison Bank vs. Alden, 129 U. S., 373; Thornton vs. Wabash R. R. Co., 81 N. Y., 462; King vs. Barnes, 109 N. Y., 267, and Ins. Press vs. Montauk Wire Co., 103 App. Div., N. Y., 472.

Spaulding vs. North Milwaukee Town Site, 106 Wis., 481, while apparently without bearing upon the question for which it is cited, is pertinent in its ruling, at page 480, that, in order to enable a corporation to sue and recover secret profits from its promoters for buying land at one price and selling it to the corporation at a higher, it must have been deceived and misled into paying the excessive price; that "a corporation as an entity cannot be deceived save as *some* of the individuals composing it are deceived," and that there must "be actual misleading of *some of their associates*, either by their affirmative words or acts or by their silence." In other words, the case is an authority supporting the decree of the court below in the case at bar.

So in A. R. L., T. & C. Co. vs. W. L. R. & T. Co., 1[illegible] Col., 599, another citation from the appellant's brief without apparent relevancy otherwise to the case at bar, the court declared it to be "an elementary principle that a shareholder must protect his interests in a corporation through the corporate organization, if possible," and that it is only when the corporation refuses to sue that he may himself maintain an action. "It is a part of the contract of sub-

scription of a shareholder that the affairs of the corporation shall be governed and controlled by its directors or trustees, or other duly authorized agents."

So Cook on Corporations, 6 Ed., Sec. 651, p. 1888, while, read in the light of its citations (Stratton vs. Pines, 126 Fed., 968; S. C. 135 Fed., 439), without application to the present case for the proposition for which it is cited, at pages 16-17 of the brief, declares: "The corporation cannot be compelled to pay to the promoters such part of the purchase price as they were to have for their profits, where they misrepresented the price which the original owner of the property was to receive."

The decree below, it is submitted, was without error, and should be affirmed.

J. J. DARLINGTON,
*Solicitor for Appellee.*